IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No.

WILLIAM RUBIN,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner William Rubin respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit entered on September 6, 1979.

Opinion Below

The opinion of the Court of Appeals, which is not yet officially reported, is annexed hereto as Appendix A. The Judgment of the Court of Appeals was stayed pending the determination of this petition. A copy of the Judgment of the District Court is annexed hereto as Appendix B.

Jurisdiction

The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

Questions Presented

1. Whether a pledge of stock to a bank as collateral for a bank loan is an "offer or sale" of a security under 15 U.S.C. § 77q(a) (Securities Act of 1933).

2. Where a Government agent testified that petitioner charged with having conspired with a co-conspirator to submit a financial statement to a bank which was false in that it gave credit for two worthless $100,000.00 checks signed by the co-conspirator, allegedly admitted knowing at the time of the offense that the co-conspirator had previously served time in jail for passing bad checks, was the Government required under *Brady* v. *Maryland,* 373 U.S. 83, 83 S.Ct. 1194 (1963), to disclose that it possessed the co-conspirator's criminal record and that that record reflected no such conviction?

3. Did Rule 801(d)(1)(B) of the Federal Rules of Evidence apply a limitation only to the use of prior consistent statements as affirmative evidence but not to such statements when used only for rehabilitation of a witness?

Statutory Provisions

Title 18, United States Code

Section 371

"If two or more persons conspire either to commit any offense against the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both.

Title 15, United States Code

Section 2(3)

"The term 'sale' or 'sell' shall include every contract of sale or disposition of a security or interest in a security, for value."

Section 3(a)(13)

"The terms 'by' and 'purchase' each include any contract to buy, purchase, or otherwise acquire."

Section 3(a)(14)

"The terms 'sale' and 'sell' each include any contract to sell or otherwise dispose of."

Section 77q(a)

"It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser."

Section 77x

"Any person who willfully violates any of the provisions of the subchapter, or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this subchapter, makes any untrue statement of a material fact or omits to state any material fact required to be stated thereon or necessary to make the statements therein not misleading, shall upon conviction be fined not more than $5,000 or imprisoned not more than five years, or both."

Statement of the Case

Petitioner was indicted on January 27, 1978 in three counts. Count 1 charged a conspiracy under Section 371 of Title 18, U.S.C., to violate (a) Section 17(a) of the Securities Act of 1933 (77q(a) and 77x of Title 15, U.S.C.), (b) Section 77e of Title 15, U.S.C., (c) Sections 1014 and 2 of Title 18, U.S.C., and (d) Sections 1341 and 1343 of Title 18, U.S.C. Counts 2 and 3 charged violations of Sections 1014 and 2 of Title 18, U.S.C., and violations of Sections 77q(a) and 77x of Title 15, U.S.C., respectively.

The part of the conspiracy which is at issue here is that which charged a violation of Sections 77q(a) and 77x of Title 15, U.S.C. As part of the objects and means whereby that part of the conspiracy was committed, the indictment charged that the fraud in obtaining loans from the Bankers Trust Company occurred by pledging as collateral to said bank common stock of All-State Insurance Company, Satellite Systems Corp., General Investment Corp. and Marlin International Company.

Loans totaling $475,000.00 were made by Bankers Trust Company to Tri-State Energy Company over a period beginning in October, 1972 up to and including the middle of December, 1972, and said common stock was pledged during the same period and thereafter up to January, 1973. Petitioner was employed by Tri-State Energy Company. Tri-State Energy Company defaulted in payment of the notes to the bank on March 5, 1973. The bank thereafter sued petitioner and others on the notes (T. 1129*).

The trial began May 8, 1978 and was completed May 26, 1978. At the conclusion of the Government's case, the Government withdrew that part of the conspiracy charging a violation of Section 77e, Title 15, U.S.C. The jury convicted the petitioners on Count 1, acquitted him on Count 3, and did not reach a verdict on Count 2, which was then dismissed. By an opinion filed September 6, 1979, the Court of Appeals in a split decision affirmed the conviction. Timely petitions for rehearing and a suggestion for a rehearing *en banc* were denied on November 20, 1979. By Order of the Court of Appeals previously issued on October 10, 1979, the Court of Appeals stayed the issuance of the mandate pursuant to Rule 41(a) of the Federal Rules of Appellate Procedure in the event the peti-

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* The letter "T" followed by a number designates page reference to the transcript of the proceedings in the District Court.

tion for rehearing was denied, pending application to this Court for a writ of certiorari.

Petitioner had moved pre-trial in the District Court, among other things, to "strike from Count 1 the allegations charging as objects of the conspiracy violations of Sections . . 77q(a) and 77x of Title 15, U.S.C. . . . insofar as they purport to allege that pledges of the stock referred to constitute an offer or sale of a security within the meaning of those sections." (Paragraph 2(a) of the affidavit of petitioner's counsel in support of the motion addressed to the indictment). The District Court denied the motion on the authority of *United States* v. *Gentile*, 530 F.2d 461 (2d Cir. 1977), *cert. denied* 426 U.S. 936 (1976). The District Court denied it again at the conclusion of the Government's case (T. 1554). The District Court instructed the jury that the Government contended the evidence demonstrated that the conspiracy had as its objective the violation of Section 77q(a) of Title 15, U.S.C., and Sections 1014, 1341, and 1343 of Title 18, U.S.C. (T. 2631). The District Court further instructed that the Government must prove that it was the purpose of the conspiracy either to violate Section 77q(a) or Section 1014 or Section 1341 or Section 1343 or any combination of these four sections (T. 2631). With respect to Section 77q(a) of Title 15, U.S.C., the District Court further, instructed the jury:

> "I charge you as a matter of law that the pledge of securities with the bank is an offer and sale for the purpose of this Act." (T. 2669)

Petitioner urged in the Court of Appeals that the action of the District Court in holding that a pledge of securities constituted an offer and sale under Section 77q(a) was in error, asked the Court of Appeals to review and

alter its previous opinion in *United States* v. *Gentile, supra,* and to adopt the Court of Appeals' opinion in the Fifth Circuit in *McClure* v. *First National Bank of Lubbock, Texas,* 497 F.2d 490 (5th Cir. 1974), *cert. denied* 420 U.S. 930 (1975) (Point V, petitioner's brief on appeal, p. 63). The Government in opposition urged that petitioner's argument be rejected because *United States* v. *Gentile, supra,* was correctly decided and that the conviction should therefore be upheld (Point IX, Government's brief, p. 79). The Court of Appeals did not address the point in its Opinion.

Reasons for Granting the Writ

1. The decision of the Court below is in direct conflict with decisions of the United States Courts of Appeals for the Fifth and Seventh Circuits, and these Courts have expressly rejected each other's reasonings and holdings.

The importance of this issue was recognized by this Court last Term when it granted certiorari in *Bankers Trust Company* v. *Mallis,* 431 U.S. 928, 97 S.Ct. 2630, 53 L.Ed. 243, to review a holding of the Court of Appeals for the Second Circuit that a cause of action will lie against the bank pursuant to Section 10(b) and Rule 10(b)-5 of the Securities and Exchange Act of 1934 for fraud in connection with the purchase and sale of a security because the bank became a "purchaser" by virtue of its acceptance of a pledge of securities as collateral for a loan. This Court withdrew its grant of certiorari, however, when respondent during oral argument "took the position that 'the mere release of a pledge is [not] a sale' . . . [and] urged that the judgment of the Court of Appeals be affirmed on a theory which differed from the

reasoning of the Court of Appeals in reversing the District Court . . ." —— U.S. ——, 98 S.Ct. 1117, 1121-1122 (1978).

Since the decision in *Bankers Trust Company* v. *Mallis, supra,* the conflict between the Courts of Appeals has widened. The Courts of Appeals for the Fifth and Second Circuits have rejected the reasoning and decisions of each other on the issue as to whether fraud which occurs in connection with the acceptance of a pledge of common stock is an offer to sell or a sale or purchase under the anti-fraud provisions of the 1933 or 1934 Securities Act. In their path other Circuits have likewise divided as to whether Congress intended that a mere pledge of securities as collateral for a loan constitutes a sale or purchase under the anti-fraud provisions of the 1933 and 1934 Acts.

These later decisions of the Courts of Appeals have dealt basically with the same issue although they involved civil fraud and not criminal actions. The issue is basically the same, we submit, as made abundantly clear in *Mallis* v. *Federal Deposit Insurance Corp.*, 568 F.2d 824, 829 (2d Cir. 1977), (before this Court) *sub nom Bankers Trust Company* v. *Mallis, supra,* where the Court of Appeals said:

> "The fact that Gentile was a criminal case in which civil standing was not an issue does not diminish its presentation as a precedent with respect to the Section 10(b) claim before us. The existence of a 'sale' is as essential to a criminal prosecution for violation of Section 17(a) as it is to a civil action under that section. We find no basis on the face of either the 1933 Act or the

> 1934 Act for denominating a pledge as a 'sale' for criminal but not for civil purposes."*

In determining whether acceptance of a pledge of stock as collateral is a sale of a security under Section 77q(a) of the 1933 Act or a purchase or sale under Section 10(b) and Rule 10(b)-5 of the 1934 Act, the Court of Appeals of the Fifth Circuit in *National Bank of Commerce* v. *All American Assurance Co.*, 583 F.2d 1295, 1296 (5th Cir. 1978), held:

> ". . . that a commercial loan on a promissory note with securities pledged as collateral is not a protected security transaction under the federal antifraud statute . . ."**

The Court of Appeals explicitly rejected the contrary reasoning of the Court of Appeals for the Second Circuit. It stated:

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* The existence of other objects of the conspiracy in the instant case in addition to the alleged violation of Section 77q(a) does not avoid the issue since it is fundamental, as this Court held in *Yates* v. *United States*, 354 U.S. 298, 312, 77 S.Ct. 1064, 1073 (1957), that:

> "[T]he proper rule to be applied is that which requires a verdict to be set aside in cases where the verdict is supportable on one ground, but not on another, and it is impossible to tell which ground the jury selected. Stromberg v. People of State of California, 283 U.S. 359, 367-368, 51 S.Ct. 532, 535, 75 L.Ed. 1117; Williams v. State of North Carolina, 317 U.S. 287, 291-292, 63 S.Ct. 207, 209-210, 87 L.Ed. 279; Cramer v. United States, 325 U.S. 1, 36, 65 S.Ct. 918, 935, note 45, 89 L.Ed. 1441."

** For purposes of this issue the Court of Appeals noted that although slight differences in wording exist between the 1933 and 1934 Acts' definition of these terms, that is, purchase, sale or offer to sell, the definitions "are functionally equivalent and are for the purposes of this case so treated." 583 F.2d *supra* at 1298.

"*Gentile* and *Mallis*, . . . can hardly be distinguished from the facts in the instant case and are contrary to the decision reached here. In these cases, the Second Circuit held that a pledge constitutes a sale for the purpose of § 17(a) of the 1933 Act, 15 U.S.C.A. § 77q(a) and § 3(a)(14) of the 1934 Act, 15 U.S.C.A. § 78c(a)(14), respectively. The decisions were grounded upon the rationale that

> the pledgee assumes a very real investment risk that the pledged securities will have continuing value, a risk that is identical in nature to the risk taken by investors which serves as the indisputable basis for statutory regulation of securities transactions.

United States v. *Gentile*, 530 F.2d 461, 467 (2d Cir.), *cert. denied* 426 U.S. 936, 96 S.Ct. 2651, 49 L.Ed.2d 388 (1976).

"This rationale might be a persuasive argument that the federal securities laws ought to encompass pledges, as well as purchases and sales. It does little to support a decision that they in fact do cover pledges. Congress can be presumed to know the difference between a collateral pledge transaction and a sale and purchase. If it had intended to cover both, it could have easily done so by words traditionally used to differentiate between the two.

"The holding that the mere pledge of a security as collateral for a loan does not constitute a sale or purchase of a security within the meaning of the federal securities laws appear sound. The federal securities acts are designed to protect investors. This purpose is not affected by a pledge of stock. As Professor Loss has stated, 'federal legislation

> was hardly needed for privately negotiated pledge transactions between borrowers and lenders.' L. Loss, Securities Regulation 649 (2d ed. 1961). The pledgee, unlike a securities purchaser, has a remedy on the note itself against makers and guarantors." 583 F.2d *supra* at 1299-1300.

In reaching this conclusion the Court of Appeals followed its prior decisions in *Reid* v. *Hughes,* 578 F.2d 634, 683 (5th Cir. 1978), which likewise held that a mere pledge of a security does not constitute a purchase or sale under Section 10(b) and Rule 10(b)-5, and *McClure* v. *First National Bank of Lubbock, Texas,* 497 F.2d 490 (5th Cir. 1974), *cert. denied* 420 U.S. 930, 95 S.Ct. 1132, 43 L.Ed.2d 412 (1975), to the same effect. The Court of Appeals also cited this Court's opinion in *United Housing Foundation* v. *Forman,* 421 U.S. 837, 95 S.Ct. 2051, 44 L.Ed.2d 621 (1975), to the effect that

> "('[w]ith the exception of the Second Circuit, every Court of Appeals has rejected the literal approach urged by respondents.' 421 U.S. at 849, n. 14, 95 S.Ct. at 2059, citing with approval McClure, among others)."

Also noting that the Court of Appeals for the Second Circuit in *Gentile* and *Mallis* "adopted a literal reading of the definition of "sale" in Section 2(3) of the 1933 Act and Section 3(a)(13) of the 1934 Act, the Court of Appeals for the Seventh Circuit in *Lincoln National Bank* v. *Herber,* 604 F.2d 1038, 1044 (1979),

> "reject[ed] the approach of the Second Circuit, . . . agree[ing] with the Fifth Circuit's position in *National Bank of Commerce of Dallas* v. *All American Assurance Co.,* 583 F.2d 1295 (5th Cir. 1978), and *McClure* v. *First National Bank of Lubbock,* 497 F.

> 2d 490 (5th Cir. 1974), *cert. denied,* 420 U.S. 930, 95 S.Ct. 1132, 43 L.Ed.2d 402 (1975), that a 'sale' of the securities does not occur at the time the securities are pledged."

The conclusion of the Court of Appeals for the Seventh Circuit is worth noting:

> "In sum, the legislative history of the 1933 and 1934 Acts is devoid of any indication of an intent to regulate pledges of securities; the Second Circuit decisions extending the Acts to such transactions are distinguishable, and to the extent they are not we disagree with their conclusion that a pledgee of stocks takes an 'investment' risk; state law adequately covers the area; and recent Supreme Court decisions have manifested a reluctance to expand the federal securities laws absent a clear indication of Congressional intent or a need to do so to accomplish the purposes of the legislation. We therefore hold that a pledge of securities is not a 'sale' for purposes of invoking the antifraud provisions of the 1933 and 1934 Acts." 604 F.2d *supra* at 1045

On the other hand, the Court of Appeals for the Sixth Circuit in *Mansbach* v. *Prescott, Ball & Turben,* 598 F.2d 1017, 1028 (6th Cir. 1979), addressing the same issue under Section 10(b) and Rule 10(b)-5, said:

> "We note a split of authority on the question but we follow those cases holding that a pledge is a 'purchase or sale.'"

The Court of Appeals analyzed the reasoning and decisions of the Second Circuit in the *Gentile* and *Mallis* cases, as well as those of the Fifth Circuit in *National Bank of Commerce* v. *All American Assurance Co.,* and *McClure* v. *First National Bank of Lubbock, Texas,* concluding:

> "[W]e think those from the second circuit are better reasoned and we follow them here. They are sufficient authority to hold that the pledge of Mansbach's bonds to PBT constituted a 'purchase or sale or securities.'" (598 F.2d *supra* at 1039).

Sufficient divergence of opinion exists between the Courts of Appeals on this issue as to what Congress intended to warrant the issuance of a writ to the Court of Appeals for the Second Circuit. Contrary reasoning by the Courts of Appeals for the Fifth and Seventh Circuits, we respectfully submit, is more consonant with the purpose of the Securities Acts as intended by Congress and with the principles announced by this Court in *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 95 S.Ct. 1917, 44 L.Ed. 2d 539 (1975). Those decisions support the conclusion that the Court of Appeals for the Second Circuit has unduly, improperly and erroneously extended the definition of a sale under 77q(a) of Title 15, U.S.C., to include the mere acceptance of a pledge of securities as collateral for a loan.

An additional but equally important reason to issue the writ, we respectfully submit, is that the petitioner had no warning whatever that his alleged conduct in pledging securities as collateral for a bank loan or aiding and abetting such conduct could reasonably constitute a violation of Section 77q(a) of Title 15, U.S.C. At the time of petitioner's alleged criminal acts in 1972 and 1973 *Gentile* had not been decided. The Second Circuit's opinion in *SEC* v. *Guild Films,* 279 F.2d 485 (2nd Cir. 1960) cert. denied sub. nom. *Santa Monica Bank* v. *SEC,* 364 U.S. 819, 81 S.Ct. 52 (1960), was considered so uncertain in scope and unclear in decision that a district court held that a mere pledge of the shares of a foreign corporation was not a purchase or sale of securities within the context of

Section 10(b) and Rule 10(b)-5. *Investment Properties International, Ltd.* v. *IOS, Ltd.*, CCH Fed.Sec. Rep., ¶ 93,011 (1971), at p. 90,740 (SDNY 1971). Petitioner had no prior warning, to which he was entitled, that his conduct could conceivably violate Section 77q(a) as the statute was applied in this case by the Government. As this Court noted in *United States* v. *Spector*, 343 U.S. 169, 171, 72 S.Ct. 591, 593 (1952):

> ". . . a statute, plain and unambiguous on its face, may be given an application that violates due process of law, . . ."

2. The Court below, in affirming petitioner's conviction despite the prosecutor's concealment of Starns' criminal record, ignored the principles of *Brady* v. *Maryland* as set forth by this Court.

A key element of the Government's proof was the fact that a balance sheet contained in the financial statement submitted to Bankers Trust Company reflected, among Tri-State's assets, two checks, each for $100,000.00, payable to Tri-State. The payor of each of these checks was Raymond Starns. The $200,000.00 face amount of these checks was included (without specific enumeration or description) in the "cash on hand" figure in the balance sheet, although neither check had been deposited. These two checks turned out to be worthless.

The Government claimed that petitioner knew that these two checks were included in the cash figure on the balance sheet, and that he also knew that these checks were worthless. In order to attempt to establish petitioner's alleged knowledge of the worthless nature of the checks, the Government offered testimony of Agent Cox that petitioner had allegedly admitted to Cox in 1975 that peti-

tioner knew—in 1972, at the time petitioner allegedly reviewed the balance sheet— "[Starns] had served time in the penitentiary for passing bad checks." Such proof was obviously devastating: for it established that at the time petitioner allegedly reviewed the balance sheet, he knew that it included among its assets $200,000.00 of uncleared checks drawn by an individual who petitioner knew had actually been convicted of passing bad checks.

Subsequent to petitioner's conviction, during the trial of petitioner's severed co-defendants, evidence was elicited establishing that (a) petitioner could not have made the statement ascribed to him by Cox regarding petitioner's alleged knowledge in 1975 of Starns' criminal record as of 1972, and (b) the prosecution knew, at the time Cox testified, that petitioner could not have made the statement ascribed to him by Cox.

The Court below, by Order dated October 19, 1978, granted petitioner's motion to add to the record on appeal the relevant portions of Starns' testimony at the second trial. Starns (who did not testify at petitioner's trial) testified at the second trial that the only offense for which he was ever incarcerated was uttering stolen securities in 1974. Starns had been interviewed by the prosecution on May 6, 1978 prior to the beginning of petitioner's trial, for his possible use as a witness at petitioner's trial (though eventually he did not testify in the petitioner's trial). Therefore, it is clear that the prosecution knew that the substance of Cox's testimony regarding the petitioner's alleged admission—i.e., that petitioner knew in 1972 (rather than in 1975, at the time petitioner was interviewed, as petitioner attempted to suggest) that Starns had been convicted and incarcerated for passing bad checks—was false.

Petitioner claimed in the Court below that the concealment of the Starns criminal record violated the principles

announced by this Court in *United States* v. *Agurs,* 427 U.S. 97, 96 S.Ct. 2392, 49 L.Ed.2d 342 (1976), in that the Government's non-disclosure fell within the first category of violations of the rule of *Brady* v. *Maryland,* 373 U.S. 83, 83 S.Ct. 1194, 10 L.Ed.2d 215, i.e., that the Government's case included perjured testimony, that the prosecutor knew, or should have known, of the perjury, and that therefore the petitioner was entitled to a new trial since there was a reasonable likelihood that the evidence if disclosed would have affected the outcome of the trial.

Simply put, the Government introduced evidence from Agent Cox that petitioner allegedly admitted having known in 1972, at the time petitioner allegedly knew that $200,000.00 of Tri-State's "cash" was unpaid checks drawn by Starns, that Starns had previously been convicted and incarcerated for passing bad checks when in fact the Government knew that petitioner could not have had such knowledge in 1972 because that state of facts did not exist prior to 1974.

Petitioner testified and asserted his innocence at the trial. The agent's testimony concerning petitioner's alleged admission, if believed, would have clearly tended to indicate guilt on petitioner's part. The extreme importance of the agent's testimony was illustrated by the Government's brief below which asserted that the agent's testimony "clearly was probative of Rubin's [petitioner] likely knowledge of the worthlessness of these checks and his intent to defraud the bank" (Gov't Brief, p. 74). What this Court said in *United States* v. *Agurs,* 427 U.S. *supra* at 111 equally applies in the instant situation:

> "For though the attorney for the sovereign must prosecute the accused with earnestness and vigor, he must always be faithful to his client's overriding interest that 'justice shall be done.' He is the 'ser-

> vant of the law, the twofold aim of which is that guilt shall not escape or innocence suffer.' *Berger* v. *United States,* 295 U.S. 78, 88, 55 S.Ct. 629, 633, 79 L.Ed. 1314. This description of the prosecutor's duty illuminates the standard of materiality that governs his obligation to disclose exculpatory evidence."

3. Did Rule 801(d)(1)(B) of the Federal Rules of Evidence apply a limitation only to the use of prior consistent statements as affirmative evidence but not to such statements when used only for rehabilitation of a witness?

The Opinion of the Court of Appeals dealt primarily with the petitioner's claim of the erroneous admission of pretrial interview notes as prior consistent statements of Government witness Agent Cox. The Court below split on a construction of Rule 801(d)(1)(B) of the Federal Rules of Evidence. The majority rejected as a holding two prior decisions of the Court of Appeals for the Second Circuit in *United States* v. *Quinto,* 582 F.2d 224 (1978), and *United States* v. *Check,* 582 F.2d 668 (1978). These decisions had actually held, as Judge Meskill in his dissenting opinion made clear, that Rule 801(d)(1)(B) applied to prior consistent statements whether used for affirmative purposes or only for rehabilitation of a witness. Judge Friendly in a concurring opinion stated that the issue was

> "important for the future to make clear that despite the contrary dictum in *United States* v. *Quinto,* 582 F.2d 224, 233-34 (2 Cir. 1978), see also *United States* v. *Check,* 582 F.2d 668, 681 n. 40 (2 Cir. 1978), the limitations [of Rule 801(d)(1)(B)] apply only to the use of prior consistent statements as *affirmative evidence* and are not controlling when such statements are used *only for rehabilitation.*"

In reaching this conclusion Judge Friendly rejected the substantive holding in *Quinto* that prior consistent statements whether offered only for rehabilitation or as substantive evidence depend for their admission upon the proponent satisfying three conditions, as provided in Rule 801(d)(1)(B). Indeed, Judge Friendly even described as dictum what the *Quinto* panel described as a holding. Thus, stated Judge Friendly:

> "The statement in *Quinto* with respect to rehabilitation was no less dictum because the opinion characterized it as a holding. . . . A judge's power to bind is limited to the issue that is before him; he cannot transmute dictum into decision by waving a wand and uttering the word 'hold'."

Judge Friendly sought to fortify his contention that the *Quinto* holding was purely dictum by adding that the issue was not even raised in the briefs before that panel. Judge Meskill in his dissent rejected Judge Friendly's interpretation of *Quinto*. He likewise rejected Judge Friendly's characterization that the *Quinto* panel's interpretation of Rule 801(d)(1)(B) applying that rule to affirmative evidence as well as rehabilitation of a witness was dictum.

Judge Meskill quoted from the *Quinto* Court that:

> "'[W]e *hold* that the memorandum should have been excluded regardless of whether it was offered for the truth of the matters asserted therein or merely for the more limited purpose of rehabilitating the in-court testimony of [the agent].'" *United States* v. *Quinto*, 582 F.2d at 232.

Judge Meskill added:

> "I simply cannot bring myself to characterize this holding as mere 'dictum.' The fact that the parties

> in *Check* and *Quinto* did not choose to brief extensively the question whether the memorandum was admissible for purposes of rehabilitation as opposed to substantive evidence should not be used to detract from the strength of the express holding that it was not. See *Monell* v. *Department of Social Services of the City of New York,* 436 U.S. 658, 717-18 (1978) (Rehnquist, *J.,* dissenting) ('Private parties must be able to rely upon explicitly stated holdings of this Court without being obliged to peruse the briefs of the litigants to predict the likelihood that this Court might change its mind.'). *See also id.* at 709 n. 6 (Powell, *J.,* concurring) ('the mere fact that an issue was not argued or briefed does not undermine the precedential force of a considered holding')."

The Federal Rules of Evidence were enacted to secure fairness and uniformity in the administration of Trials in the Federal Courts. This split decision, we respectfully submit, will have a profound and disturbing effect on future trials as to what was intended by the enactment of Rule 801(d)(1)(B). The use of prior statements either for impeachment or consistency are vital trial techniques. To the extent they are aids in determining the credibility of witnesses, it is important that essentially precise and understandable rules be available for their use and application. A review and definitive ruling by this Court will solve what may otherwise become "a lively controversy", as Judge Friendly referred to the period before the adoption of the Federal Rules of Evidence. See *United States* v. *Herring,* 582 F.2d 535, 541 (10th Cir. 1978), in accord with *Quinto; United States* v. *Allen,* 579 F.2d 531 (9th Cir. 1978), in accord with *Quinto; United States* v. *Lanier,* 578 F.2d 1246, 1256 (8th Cir. 1978), cert. denied —— U.S. ——, 99 S.Ct. 169 (1978) in accord with *Quinto; United States* v. *Williams,* 573 F.2d 284, 289 (5th Cir. 1978), in accord with Judge Friendly.

CONCLUSION

For the above reasons it is respectfully submitted that the petition for a writ of certiorari should be granted.

Respectfully submitted,

BENDER & FRANKEL
Attorneys for Petitioner

LOUIS BENDER
SANDOR FRANKEL
Of Counsel

APPENDIX A

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 352—August Term, 1978.

(Argued November 8, 1978

Decided September 6, 1979.)

Docket No. 78-1221

UNITED STATES OF AMERICA,

Appellee,

—v.—

WILLIAM RUBIN,

Defendant-Appellant.

Before:

FRIENDLY, MANSFIELD and MESKILL,

Circuit Judges.

Appeal from a judgment of the District Court for the Southern District of New York, entered on June 30, 1978, by Judge Constance Baker Motley after a jury trial, convicting appellant of conspiracy, 18 U.S.C. § 371, to violate statutes prohibiting false statements in connection with loan applications, and

mail fraud, wire fraud and securities fraud. 18 U.S.C. §§ 1014, 1341, 1343; 15 U.S.C. § 77q(a).

Affirmed.

LOUIS BENDER, New York, New York (Sandor Frankel, Bender & Frankel, New York, New York, of counsel), *for Defendant-Appellant.*

RHEA KEMBLE NEUGARTEN, Assistant United States Attorney, Southern District of New York (Robert B. Fiske, Jr., United States Attorney, Robert J. Jossen, Assistant United States Attorney, Southern District of New York, of counsel), *for the United States of America.*

MANSFIELD, *Circuit Judge:*

William Rubin appeals from a judgment of the District Court for the Southern District of New York, entered on June 30, 1978, by Judge Constance Baker Motley, *Judge,* after a fifteen-day jury trial, convicting him of conspiracy to violate a federal statute prohibiting the making of false statements in connection with a loan application, a loan renewal, deferral of action on a loan, or substitution of security for a loan, as well as federal statutes relating to mail fraud, wire fraud and securities fraud.[1]

Rubin and four others were named in a three-count indictment handed down on January 27, 1978.

1 Respectively: 18 U.S.C. § 1014, 1341, 1343, 2; 15 U.S.C. § 77q(a). The indictment originally charged a conspiracy to violate 15 U.S.C. § 77(e) as well but this was deleted from the indictment before the case was submitted to the jury.

Count One charged all five with conspiracy as indicated above. Count Two charged Rubin and three of the others with a substantive violation of 18 U.S.C. § 1014, the false statement statute, and 18 U.S.C. § 2. Count Three charged Rubin and three of the others with a substantive violation of 15 U.S.C. § 77q(a), the securities fraud statute, and 18 U.S.C. § 2.[2]

Prior to trial the Government moved for a severance of Rubin's trial from the trials of the other defendants; the trial judge granted the motion and Rubin was tried first.[3] The jury found Rubin guilty on Count One but acquitted him on Count Three; the Government then moved to have Count Two dismissed, which was granted. Rubin was sentenced to three years in prison, but is free on bail pending disposition of this appeal. Although Rubin does not argue that there was insufficient evidence to support his conspiracy conviction, he does raise a variety of other legal claims in support of a dismissal of the indictment or a new trial. Finding no merit in these contentions, we affirm.

The present case arises out of the activities in late 1972 and 1973 of Rubin, Leonard James, C.W.

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2 Peter Crosby, Otto Sebold, Leonard James and C.W. Deaton were the other four named in the indictment. Crosby was not named in Count Two; Sebold was not named in Count Three.

3 Trial of three of the other defendants began before Judge Motley in May of 1978 and concluded a month later. Crosby was acquitted on both of the counts in which he had been named; Sebold and James were found guilty of conspiracy and one of the substantive counts. Deaton was never tried. The charges set forth in the indictment against him were not the subject of the extradition order by which his presence in the United States had been obtained. As to him, Judge Motley granted the government's application for an order of nolle prosequi. James and Sebold have appealed their convictions to this Court, #78-1346, and their appeal is presently sub judice.

Deaton, and Otto Sebold in fraudulently obtaining financing from the Bankers Trust Company and others for a failing company, Tri-State Energy, Inc. (Tri-State). The methods employed to obtain the funds included use of material misrepresentations, false documentation, worthless collateral, and bribery. Prior to becoming associated with Tri-State and with James and Deaton, who were its principal officers, Rubin, a certified public accountant and law school graduate, was a principal in North American Planning Corporation (NAPC), a brokerage firm. In June, 1972, Rubin borrowed 10,000 shares of All States Life Insurance Company of Alabama from Tri-State on Deaton's representation that the shares were freely tradeable, only to find that they were restricted and unacceptable as collateral, which led to NAPC's demise. Left without a job, Rubin, though put on notice of the fraudulent business methods used by James and Deaton, became associated with them in Tri-State[4] in the fall of 1972, and soon embarked upon the fraudulent scheme which led to the indictment in the present case.

Tri-State had recently acquired a small coal mine in Kentucky, which operated very briefly in the latter part of 1972.[5] The mining properties were used by James and Deaton as a means of obtaining loans from Bankers Trust by falsely representing that they were a viable coal operation. In addition, Tri-State

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4 Rubin was not given a stock interest in the company. Instead, he was to receive a salary, bonuses, and 20% of the profits. James was president of the company, and Deaton was called secretary-treasurer. In reality, Deaton appears to have been the "de facto chief executive officer" of the corporation.

5 The mine was under the supervision of Deaton's brothers, Jack and Robert.

acquired control of other virtually worthless publicly-owned companies, such as American Leisure Corporation, with a view to giving the appearance, on paper at least, of a thriving enterprise. Rubin's function, aside from obtaining some initial small loans from friends for the venture and negotiating some of the acquisitions, was to dress up Tri-State's financial statement in order to give it the false appearance of a company with a substantial net worth that would generate attractive profits in the future.

In October 1972, Rubin and Deaton (possibly accompanied by James), approached Leonard Ludwig, a branch manager of Bankers Trust Company, with whom Rubin had had dealings before joining Tri-State, to seek a loan for Tri-State. Ludwig refused a loan on the ground that the bank first needed evidence that Tri-State was a viable coal operation. Deaton, James and Rubin responded by preparing various materially false documents, including a financial statement regarding Tri-State's operations and conditions.

A second meeting with Ludwig on October 19, 1972, resulted in his agreeing to make a loan of $50,000 and to discuss additional loans after he had seen more Tri-State financials. Ludwig then obtained approval of the loan from John Keating, another official of the bank, as required by the bank's rules.

At either their first or second visit with Ludwig, Rubin and Deaton told Ludwig that if he took care of Tri-State it in turn would take care of him. After the second visit Rubin, Deaton, and James agreed that a payment of $1500 should be made immediately to Ludwig, to be followed by more at a later time. To accomplish this, Deaton gave Rubin a $1500 Tri-State check payable to cash which Rubin cashed

at his country club. Rubin then gave the $1500 in cash to Ludwig, adding that more money would follow. True to his word, Rubin later gave Ludwig an additional $2500 in cash at a meeting in a bar. At Ludwig's suggestion, Rubin also made two payments of $500 cash each to Keating, one by placing the money in Keating's pocket in the men's room at his Bankers Trust branch and the other in an envelope at the bank.

In addition to the loan of $50,000 which was obtained on October 19, 1972, Rubin and Deaton were able during the following six weeks to borrow $425,000 from Bankers Trust. On November 22, Tri-State renewed the original $50,000 loan for three months and borrowed another $50,000. Eight days later, Tri-State borrowed another $100,000 for three months. After another six days, Tri-State borrowed still another $275,000, also for three months.

In addition to their use of bribery of the bank's officers, Rubin, James and Deaton also used materially false financial documentation and bogus collateral to secure approval of the loans and later to prevent the bank from taking action that would precipitate Tri-State's collapse. In response to Ludwig's earlier request, a financial statement was submitted to the bank, which was materially false in several respects. For example, it listed as Tri-State's principal asset a $7.5 million receivable from a company by the name of Charter Financial, supposedly resulting from a coal purchase by that company. There was no such account receivable.[6] The statement

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6 There did exist a *conditional* contract between Tri-State and Charter Financial, and it was in fact signed by Charter Financial's president, Stanton Kahm. But that was not the contract

also showed that Tri-State had over $250,000 in cash. Of this cash amount, $200,000 was in fact attributable to two undeposited, uncashed checks drawn by one Raymond Starns on his personal checking account and in the possession of Tri-State. The financial statement also reflected $180,000 worth of coal inventories. In fact, Tri-State had far less.

The October 20th statement had initially been prepared by an outside accountant named Max Englander. Englander's original draft balance sheet showed the Charter Financial contract as an asset but failed to show any liability. Rubin corrected this by offsetting the "asset" with a liability for income taxes of $3.75 million. Englander's draft also had itemized the company's available cash, dividing it into $200,000 cash on hand and a little over $50,000 in various banks; the draft identified the $200,000 as consisting of the two checks written by Raymond Starns. Rubin "corrected" these entries by consolidating them and eliminating reference to the Starns checks. Rubin made no change relating to the coal inventory, but there was evidence from which the jury could infer that he knew at the time that the Kentucky mine was only minimally operational and that the coal inventory figure was overstated. Englander testified that, after Rubin had made his corrections, Deaton instructed him to make additional changes so as to increase the company's net worth above what it would have been using Rubin's computations. It is the Government's position that, although the copy of the statement that Rubin worked

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shown to the bank. To the contrary, a signed, unconditional contract between the two companies was offered to the bank. Kahm's signature on that contract was forged.

on was not the one ultimately turned over to the bank, Rubin's work on the statement made the Charter Financial asset appear more regular than it really was and eliminated the possibility of the bank's becoming suspicious about the company's available cash.[7]

From the beginning of its relationship with Tri-State, Bankers Trust had made it clear that any loans must be collateralized. As collateral Tri-State turned over to the bank a certificate for 400,000 shares of American Leisure stock, which was in Tri-State's name, unregistered, and bore a restrictive legend. Keating recognized that unregistered stock was of doubtful value as collateral in the event of default and told Tri-State that he would accept the stock but preferred marketable collateral. He was then assured by Rubin and Deaton that Tri-State would present such collateral and was promised that the restriction on the American Leisure stock would be removed.

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7 Besides this financial statement, Tri-State presented Bankers Trust with a written projection of Tri-State's revenue, a document which Keating and Rubin apparently discussed and which Keating used as support for his decisions to approve the loans. This document projected a gross income of $540,000 based on anticipated sales of coal to companies by the name of Continental Coal Corporation and Repoca Resources and on a long-term export contract with a German firm by the name of Roland Werkstatten. In fact, there had never been any discussions with Repoca, and the contract with the German firm was a sham, having been prepared by Rubin's co-defendant Otto Sebold, a representative of the German firm who used office space at Tri-State. From all of the surrounding circumstances the jury could infer that Rubin knew that the revenue projection was false and misleading.

In addition, Rubin furnished to the bank a map overstating Tri-State's coal reserves, a forged letter of intent from Repoca, and a statement valuing Tri-State's coal reserves at $3 per ton in place when the actual value of such coal was only $1 per ton.

Appendix A

Between October of 1972 and January of 1973 Tri-State pledged the stock of several other companies as collateral, including stock in All States.[8] The stock was represented to Keating to be marketable, owned by Tri-State and to have been obtained through the sale of coal rights to the Kentucky mine. In fact, as Rubin knew, most of the collateral was not owned by Tri-State but had been "rented" by it for a fee. Moreover, the shares were virtually worthless, since none of them were freely tradeable, five of the stocks had never been registered, the sixth had not been registered since 1944, and the American Leisure shares bore a restrictive legend. Rubin had participated in attempting to establish a misleading value for the All States shares by having the stock placed in the over-the-counter "pink sheets" by a friend in a brokerage house, Marshall Murray & Co. The stock, however, was virtually never traded during the four month period from October, 1972, to February, 1973, when it was so carried.

Each of the notes signed by Tri-State and given to Bankers Trust for the loans contained conditions which made them collectible before maturity if any representation in connection with the loans proved to be "untrue or incomplete," if there was an "adverse

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8 The following additional stocks were pledged with Bankers Trust on the dates indicated:

2,000 shrs	All States 11/10/72
20,000 shrs	Marlin Investment Company, 11/22/72
100,000 shrs	Management Dynamics, Inc., 12/6/72 (returned to Tri-State a few days later)
175,000 shrs	General Investment Corp., 12/10/72
50,000 shrs	Satellite Systems Corp., 1/19/73

All shares were pledged as collateral for each of the loans.

change" in Tri-State's condition, or if a legal proceeding should be commenced against Tri-State by a judgment creditor. As Tri-State began to sag its principals reassured the bank that all was well. These reassurances were quite plainly untrue. In December of 1972 the Tri-State payroll checks for the Kentucky mine began to bounce; by Christmas the mine was closed and the Deaton brothers had left town. By early January the company was dishonoring checks throughout its operation. In one way or another, these developments came to the bank's attention.

Beginning in January or February of 1973, Keating had the bank's credit department check into the various items of collateral that had been pledged by Tri-State as support for the loans. He also began to make sure that the bank had sufficient documentation on the collateral to support a foreclosure if that turned out to be necessary. Buttressed by reassurances from Tri-State that the company was not only in no financial difficulty but was in fact prospering, and despite all the bad news that seemed to swarm around the Tri-State transactions, Keating decided that the best way to prevent a loss to the bank, as well as to save himself from a potentially embarrassing situation, was to consolidate the four outstanding time loans into a single demand note at a higher interest rate. On February 26, 1973, amid continuing assurances by Rubin, Deaton and James as to Tri-State's prosperity, a demand note was executed by James on behalf of Tri-State. The loans were not called.

Two days later the bank received an inquiry from the United States Justice Department asking for information about Tri-State. On March 5 the bank de-

manded full payment within three days. This demand went both unpaid and unenforced and on May 14, 1973, Deaton met with several people from the bank in an effort to forestall payment of the note. Deaton even asked for an additional loan, to be used to develop Tri-State's assets to the point of being able to pay off the note. The bank declined and initiated a lawsuit against Tri-State. Subsequently, Rubin signed a confession of judgment against himself but he then filed a petition in bankruptcy. In all, the bank has recovered about $2,500 of the $475,000 (plus interest and expenses) due from Tri-State.

The Government investigation led to its interrogation of Rubin, beginning in July 1973. Rubin was told of the nature of the Government's investigation, was advised to obtain counsel, and was asked to consider cooperating with the Government by furnishing evidence against his co-conspirators on the informal understanding that the Government was "not going to let him walk away" but would consent to his pleading guilty to one felony count. Rubin decided to cooperate, after consulting his counsel, with whom he appeared in July, 1973, whereupon he was advised of his constitutional rights and interrogated in his counsel's presence. From July 1973 to July 1976, Rubin was interviewed approximately 13 times by various Government agents (including Edward J. Levitt) and attorneys. No written statement was taken from him but some of the agents took extensive notes during the interviews, cryptically summarizing the substance of what Rubin recounted, with quotes here and there. These notes, totalling more than 70 pages, were later marked Government Exhibit (GX) 66 for identification at the trial of

Rubin. Since Rubin was at the time of the interviews a cooperating prospective defendant expected to plead guilty, no effort was made to obtain his signature to or his formal approval of the notes. As time went on, however, Rubin ceased cooperating with the Government and decided to stand trial, apparently after he was unsuccessful in renegotiating his arrangement with the prosecution to one whereby he would be granted immunity in lieu of pleading guilty to one felony count.

On January 27, 1978, an indictment was filed in the District Court for the Southern District of New York, naming Rubin and various co-conspirators, including James, Deaton, Otto Sebold, and Peter Crosby. Upon the Government's motion a severance of Rubin from his co-defendants was granted for the reason that his pre-trial interview statements, which the Government proposed to introduce, would create problems under *Bruton* v. *United States*, 391 U.S. 123 (1968), as to his co-defendants. At the trial of Rubin the Government, as part of its direct case, introduced testimony of various witnesses, including Ludwig, Keating, Englander, Levitt and government agents. One of the principal witnesses was Internal Revenue Agent Thomas Cox, who was present at 12 of the 13 interviews of Rubin and testified to Rubin's detailed incriminating account of the Tri-State fraud upon Bankers Trust. In his defense, Rubin took the witness stand and called various witnesses in an effort to show that he had not intended to use Tri-State as an instrument of fraud, but had acted in a good faith effort to promote Tri-State as a viable business.

Appendix A

DISCUSSION

Admission of Agent's Interview Notes

Rubin's most serious claim is that the trial judge committed reversible error in admitting into evidence, upon the Government's redirect examination of Agent Thomas Cox, a few of the more than 70 pages of notes made by other government agents present at the preindictment interviews of Rubin, after Cox had used them on his direct examination to refresh his recollection and Rubin's counsel had used them extensively on his cross-examination of Cox. Although Cox had not personally made the notes, he had been present at the interviews recorded in the notes, had participated in the interrogation of Rubin, examined the notes at the conclusion of each interview and testified that the notes accurately reflected what had been said at the interviews attended by Cox. Thus Cox, in effect, adopted the notes as his own.

Upon direct examination, Cox testified to Rubin's incriminating history of his becoming associated with James and Deaton in Tri-State, the poor state of Tri-State's business and finances, their fraudulent negotiation of the loans from Bankers Trust to Tri-State, the bribery of Ludwig and Keating, and their preparation and use of false Tri-State financial statements, other false documentation and bogus collateral to obtain the loans and lull the bank into taking no action to call the loans.

In a prolonged and somewhat confusing cross-examination of Cox, Rubin's counsel, Louis Bender, though he had repeatedly objected to Cox's direct testimony on the ground that it was based on the

agent's interview notes rather than on his own independent recollection, now adopted the strategy of using the notes extensively in an effort to show that Cox's present testimony was either inconsistent with the notes or not supported by them. In pursuing this line of inquiry Bender, although the interview notes were not in evidence, frequently read verbatim excerpts which, when taken out of context, tended to indicate that Rubin's interview admissions had not been as incriminating as those attributed to him by Cox and then elicited from Cox a confirmation that Bender had accurately quoted the portions so read by him to the witness. (See e.g. Tr. 762, 767-68, 784, 798, 800, 801, 807, 811, 816-17, 819, 820, 852, 864, 867, 872). When a suggestion was made by the prosecutor and the Court that if Bender was going to continue reading from the notes perhaps they should be introduced as evidence, Bender demurred, claming a right "to read a prior inconsistent statement, if it is." Tr. 763. Although it was then agreed that the notes would be so used only with respect to matters as to which Cox had relied upon them rather than on his independent recollection, Tr. 764-65, Bender continued to quote from the notes as he had done previously.

Some examples of the foregoing attempted impeachment of Cox's credibility are found in the cross-examination of him with respect to (1) whether James had attended the first meeting with Ludwig at Bankers Trust at which Rubin and Deaton sought a loan to Tri-State, Tr. 758-59, (2) whether Rubin told Ludwig that he would be taken care of if the loan were approved, Tr. 768-69, and (3) whether Rubin had known in October, 1972, that Raymond

Starns, whose undeposited checks for $200,000 were carried as "cash" on the Tri-State's October 20, 1972, financial statement used to obtain some of the loans, had been imprisoned on certain charges. Tr. 784. With respect to most of these matters Bender quoted portions of the interview notes that appeared possibly to be inconsistent with testimony given by Cox on direct, thus furnishing the jury with these portions. For instance, Cox on direct attributed to Rubin an admission that at his first meeting with Ludwig, Rubin had said to Ludwig, "Look, Ray, if you can see your way clear to help us, we will take care of you." Tr. 667. On cross Bender pointed out that while the interview notes contained the statements in quotes "If you take care of us we will take care of you" they were followed by the notation, not in quotes, "No—Don't know," Tr. 767-69. Cox could not recall Rubin's making the latter statement. Bender's purpose in bringing it out, however, was manifest: to cast doubt on Cox's veracity.

Turning to the four exhibits forming the basis of appellant's present claims (GX 66A, 66B, 66C, and 66D) the first, 66A, consisting of two pages, represents a portion of Agent Levitt's notes of an October 10, 1974 interview of Rubin in which he recounted events immediately following Ludwig's meeting on October 20, 1972, with Rubin, Deaton and James at the bank, at which Ludwig approved the first $50,000 loan to Tri-State. The notes start with the word "Pay-off" and then describe the discussions between Rubin, Deaton and James, their decision to pay Ludwig $1500 immediately, the drawing of the check in that amount to cash, the cashing of the check by Rubin, his payment of the proceeds

to Ludwig and his report to Deaton and James. The detailed notes appear completely consistent with Cox's testimony on direct. However, on cross, before the notes were offered, Bender pointed out to Cox that he could not say whether Rubin had used the word "Pay-off" in the interview, although Rubin did state that he had given the money to Ludwig.

Upon redirect the Government offered GX 66A as a "prior consistent statement" by Cox regarding what he had been told by Rubin at the October 10, 1974, interview, to which Rubin objected on the grounds that the notes were not what Rubin had said but the agents' characterization of what Rubin had said and that the notes should in any event be introduced through the agent who made the notes (Levitt) rather than through Cox. These objections were overruled. The excerpt from the notes was received and read to the jury.

The next exhibit objected to on this appeal, GX 66B, is a typed excerpt from notes of a February 14, 1975, interview of Rubin in which he discussed the Tri-State $7.5 million receivable from Charter Financial which had been included as an asset, supposedly resulting from a coal purchase by that company from Tri-State, in the latter's false financial statement submitted by Rubin to Keating of Bankers Trust in support of Tri-State's application for a loan. When checking the balance sheet, Rubin had told Englander of Tri-State to include a liability for income taxes of $3,750,000. The Government's theory at trial was that Rubin knew that the listing of the Charter Financial asset was fraudulent (as indeed it was) and that his suggestion that a liability be included on the balance sheet operated to make the asset look more

"regular," thus preventing the bank from becoming suspicious.

On direct, Cox testified that Rubin had said during the interview that the "assets involved in [the balance sheet] were worthless, and he knew it," Tr. 672, and that "[a]t the time he was given this balance sheet to approve or to comment on he knew that that balance sheet was totally false," Tr. 673. Cox also referred to Rubin's putting in the tax liability, but said it had not been put in against any particular asset. Tr. 668. He testified that the only matters Rubin had talked about relating to the balance sheet and the value of the assets were "those two items," meaning the Raymond Starns' checks totalling $200,000, Tr. 674, and that the only contracts that Rubin had talked about were contracts that had been purportedly made with German concerns. There was no reference to the Charter Financial contract.

On cross Cox, in response to questions by Bender about the Charter Financial "contract," testified that it had been brought up at one of the interviews at which he was present but that he (Cox) had not been "too interested in it," Tr. 809, and that Rubin had indicated that he was not deeply involved with Charter Financial. Tr. 809-10.

On redirect the Government introduced as GX 66B the third paragraph of page 3 of the typed notes of the February 14, 1975, interview of Rubin "as a prior consistent statement of the witness," Tr. 885, which reads:

> Deaton did enter into one deal with Charter Financial whose representative was Stanley Kamm of Milwaukee, Wisc. Apparently there

> was some sort of guarantee of the Home Insurance Co. on Maiden Lane attached to the executory contract which Tri State had in its files. The contract was not executed, but was signed by Mr. Kamm. Also Kamm had previously done some business had some connection with Mortgage Guaranty of Milwaukee, MAGIC.

When Bender objected on the ground that the witness had not given any testimony contradicting the agent's notes, the prosecutor argued the excerpt was admissible "to show Mr. Rubin's state of mind," whereupon it was admitted and read to the jury.

GX 66C is an excerpt from the agents' notes of a January 9, 1975, interview of Rubin dealing with his statement regarding Raymond Starns, who had written two $100,000 checks that were turned over to Tri-State and, although not cashed by it, were carried by it as "cash" on the October 20, 1972, Tri-State false financial statement used by Rubin to obtain the bank loans. The original draft of the balance sheet showed the cash entry as being represented by the two Starns checks in Tri-State's possession. However, Rubin changed the cash entry by consolidating the cash amount and eliminating reference to the Starns checks.

Cox testified as follows as to Rubin's explanation for the change in the balance sheet: "He made a comment about the two checks because Raymond Starns who wrote these two checks in blank that were never negotiated, Rubin knew that he had served time in a penitentiary for passing bad checks." Tr. 669. Bender immediately objected to Cox's use of the word "knew," arguing that Cox was

implying that Rubin had known at the time of his work on the balance sheet that Starns had spent time in jail for passing bad checks. Bender's point was that, at most, Rubin had said that he knew at the time of the interview that Starns had been imprisoned on such charges. Cox insisted, however, that Rubin had said at the interview that he knew at the time of working on the balance sheet that the checks by Starns were probably worthless because he knew at that time that Starns had been in jail for passing bad checks. Tr. 669-74, 784.

On cross-examination, Bender read to Cox the following excerpt from the interview notes dated February 14, 1975: "According to Rubin, Raymond Starns is now in jail in New Orleans, possibly a bad check charge." Tr. 784. Cox then acknowledged that the term "now" in the excerpt referred to the date of the interview and not to the time when the balance sheet was prepared or the financial statement was offered to the bank. Tr. 784. Cox steadfastly maintained, however, that the October 14 note was not inconsistent with his earlier testimony regarding Rubin's knowledge of Starns' imprisonment. After a recess, Cox said that he could not find anything in the interview notes to support his version of Rubin's knowledge, but he did refer to page 12 of the notes dated January 9, 1975, and mistakenly conceded that that page was the one read to him by Bender and the only place in the notes where there was reference to Rubin's comments on Starns' jailing.

The Government took advantage of this discrepancy on redirect, suggesting that on January 9 Rubin had not said that Starns *was then* in jail for passing bad checks but that Starns *had been* jailed on such

charges. Cox agreed with this interpretation. The Government then offered the January 9 notes into evidence "as a prior consistent statement of the witness." Tr. 890. Bender did not object, the exhibit was received into evidence, and Cox read the entry to the jury. GX 66C states:

> Raymond Starns—2 check—? Starns & Deaton—old friends—Raymond Starns gave Deaton mine. Jail—New Orleans—bad Checks— Salt Lake.

GX 66D, two pages of agents' handwritten notes of an interview of Rubin on March 28, 1975, relates to Rubin's purchases of All States stock, allegedly made on behalf of Tri-State in order to establish a public record that would convince the bank that that All States collateral was valuable. Bankers Trust, in evaluating over-the-counter stock that was offered as collateral, consulted the price of the stock as listed in the "pink sheets" published by the National Daily Quotation Service. All States had not been listed in the pink sheets since September 27, 1972, and, accordingly, would not be viewed by the bank as valuable collateral. To remedy this situation, Deaton told Rubin to write a personal check to the Marshall Murray & Co. stock brokerage firm for the purchase of 100 All States shares. The stock was to be ordered in Rubin's, not Tri-State's, name; Rubin was reimbursed out of Tri-State's funds. The effect of this transaction was that All States appeared in the pink sheets during the time that the loans were being sought and "collateralized." Rubin acknowledged making the purchase, but denied doing so in order to bring up the pink sheet price.

On direct, Cox testified that Rubin had described this series of transactions during one of the interviews. On cross, Bender brought out the fact that Deaton was the one who had had a conversation with Marshall Murray & Co. regarding the pink sheets, and that he (Cox) had only assumed that Rubin was present during that conversation. On redirect, the Government introduced the two pages of hand-written notes "as a prior consistent statement on the subject of pink sheets." Tr. 895. Bender objected that no inconsistencies had been developed on cross; the Government responded that doubts may have been raised on cross regarding Rubin's intent and knowledge. The notes were admitted and read to the jury.

Rubin does not dispute the relevance of the agents' notes (GX 66A-D) to the issues in the case. However, relying upon our recent decisions in *United States* v. *Check,* 582 F.2d 668 (2d Cir. 1978) and *United States* v. *Quinto,* 582 F.2d 224 (2d Cir. 1978), he contends that they are inadmissible hearsay, whether offered as prior consistent statements to rehabilitate the witness Cox or to prove the facts stated, and that their admission was highly prejudicial to Rubin since the notes dealt with the main issue raised by his defense, which was whether Rubin intended his payments to Ludwig and Keating to be bribes or merely gifts that were not designed to influence their approval of the loans to Tri-State.

Rubin argues that the excerpts from the notes should have been excluded for the reason that the Government failed to satisfy the three conditions precedent to admission of prior consistent statments specified by us in *Quinto, supra,* 582 F.2d at

233-234: (1) that the prior statement be consistent with the witness' in-court testimony (2) that the prior statement be "offered to rebut an express or implied charge against him of recent fabrication or improper influence or motive," Fed.R.Evid. 801 (d) (1) (B), and (3) that the statements have been made prior to the time when the motive to fabricate arose. If Cox's adopted prior statements had been offered as substantive evidence under Fed.R.Evid. 801(d)(1)(B), the Government would undoubtedly have been obligated to meet these conditions. Whether or not some lesser standard would be required if the prior statements had been offered merely to bolster Cox's credibility as a witness may be debated, as our esteemed brother, Judge Friendly, forcefully explains, notwithstanding our indication in *Quinto* that the standards for use of such statements for rehabilitative purposes should be the same as those under Fed.R.Evid. 801(d)(1)(B), 582 F.2d at 233. It is true that prior to the adoption of the Federal Rules of Evidence we had taken a more lenient and flexible attitude toward use of prior consistent statements for rehabilitation purposes. *See, e.g., United States* v. *Lombardi* 550 F.2d 827 (2d Cir. 1977); *Appelbaum* v. *American Export Isbrandtsen Lines,* 472 F.2d 56, 60-62 (2d Cir. 1972). If the agents' notes in this case had been admitted on that limited basis, the trial judge would have been required if requested by Rubin to instruct the jury as to the limited purpose for which they were received, i.e., as bearing on Cox's credibility and not as substantive evidence, *United States* v. *Di Lorenzo,* 429 F.2d 216, 220 (2d Cir. 1970), *cert. denied* 402 U.S. 950 (1971). However, we consider it unnecessary to resolve that issue

in this case for the reason that the admission of the excerpts from Cox's adopted notes must in any event be sustained on other grounds.

Since the record reveals no objection by defense counsel to the admission of GX 66C, which dealt with the Starns checks and the time when Rubin knew of Starns' imprisonment on a bad check charge, Rubin is precluded from raising the issue on appeal. As for GX 66A, which used the term "Pay-off," to which Rubin now objects on hearsay grounds, we note that it was Rubin's own counsel who first read the word "Pay-off" from the exhibit to the jury upon his cross-examination of Cox, so that the jury was fully aware that the exhibit bore the damning word even before GX 66A was introduced. If this did not waive any objection it at least served to mitigate or eliminate any prejudice caused by the use of the word in the exhibit as later received. Aside from this opening of the door, defense counsel at no time objected to the receipt of GX 66A on the hearsay grounds urged on appeal. The sole grounds urged by him were that the exhibit contained the agents' characterizations of what Rubin had said rather than Rubin's words and that the proper witness through whom to offer the exhibit was the agent who made the notes (Levitt) rather than Cox.[9]

Neither of these specific objections is sustainable. Since Cox had, immediately following the interview of Rubin, adopted the notes as accurate and in accord with his own recollection, they could be properly treated as a prior consistent statement made by him.[10] Assuming the notes were otherwise not ob-

9 Actually Levitt, now an attorney in the Department of Justice, did testify later as a Government witness.

10 Bender's objection that the notes were not Cox's statements was not implausible when made. When Bender first tried to read

jected to, the claim that they represented "characterizations" of what Rubin had said would go to their weight rather than to their admissibility.

In short, defense counsel registered two specific objections to the exhibit, neither of which was valid. When the Government then sought to support the offer as a "prior consistent statement" there was no objection by defense counsel that the Government had failed to show a claim by Rubin of recent fabrication or improper influence or motive on Cox's part, or that the statement had been made prior to such a motive. Nor was there any answer to the prosecutor's argument to the trial judge that since Bender had sought to attack Cox's credibility by quoting "specific inconsistencies" and going to "peripheral matters" the exhibit should be received in the interest of completeness, i.e., in order to preclude Bender's later arguing to the jury that his quotations from the exhibit were "illustrative of the whole."

Rule 103(a) of the Federal Rules of Evidence provides in relevant part as follows:

> Error may not be predicated upon a ruling which admits . . . evidence unless a substantial right of the party is affected, and . . . a timely objection or motion to strike appears of record, stating the specific ground of objection, if the

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from the notes, the Government objected on the ground that the notes should be put in evidence if Bender was going to read them. Bender responded that he was only using the notes as prior inconsistent statements to impeach Cox's testimony. Judge Motley ruled that he could not so use the notes because they were not Cox's statements but statements of someone else which could not be attributed to Cox. Tr. at 763-64. At a later point Judge Motley after hearing further testimony and argument, revised this ruling.

specific ground was not apparent from the context . . . .

The reason for such a rule has been aptly summarized:

> The initiative in excluding improper evidence is left entirely to the opponent,—so far at least as concerns his right to appeal on that ground to another tribunal. The judge may of his own motion deal with offered evidence; but for all subsequent purposes it must appear that the opponent invoked some rule of Evidence. A rule of Evidence not invoked is *waived.*
>
> . . . .
>
> The function of the objection is, first, to signify that there is an issue of law, and, secondly, to give notice of the terms of the issue.
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> . . . .
>
> The cardinal principle (no sooner repeated by Courts than ignored by counsel) is that a *general objection, if overruled,* cannot avail the objector on appeal.
>
> . . . .
>
> The only modification of this broad rule is that if on the face of the evidence, in its relation to the rest of the case, there appears *no purpose whatever* for which it could have been admissible, then a *general objection,* though *overruled,* will be deemed to have been sufficient.
>
> . . . .
>
> A specific objection *overruled* will be effective to the extent of the grounds specified, and no further. An objection *overruled,* therefore, naming a ground which is untenable, cannot be availed of because there was *another and tenable ground which might have been named* but was not.

1 *Wigmore on Evidence* § 18, at 321-22, 332, 336, 339-40 (emphasis in original; footnotes omitted). *See also* McCormick, *Law of Evidence* § 52 (2d ed. 1972); 21 Wright & Graham, *Federal Practice and Procedure: Evidence* §§ 5031 *et seq.*

On a number of occasions we have spoken of the importance of this rule and the strictness with which it should ordinarily be applied. *See, e.g., United States* v. *Maultasch,* 596 F.2d 19, 29 (2d Cir. 1979) (in the absence of an "objection that clearly stated the specific ground now asserted on appeal" the claim of error is "unavailing"); *United States* v. *Moore,* 571 F.2d 76, 88 (2d Cir. 1978); *United States* v. *Del Llano,* 354 F.2d 844, 847 (2d Cir. 1965) (*en banc*); *United States* v. *Indiviglio,* 352 F.2d 276 (2d Cir. 1965) (*en banc*), *cert. denied,* 383 U.S. 907 (1966).

Regardless of Rubin's failure to object on any proper grounds, there remains the question of whether the receipt of the notes should be treated as "plain error." *See* Fed.R.Crim.P. 52(b); Fed.R.Evid. 103(d); *United States* v. *Check, supra,* 582 F.2d at 676-78 & n.28. Compare *United States* v. *Moore, supra,* 571 F.2d at 88-89, with *United States* v. *Indiviglio, supra,* 352 F.2d at 280-81. We believe not. On the contrary, GX 66A appears to have been clearly admissible under the doctrine of completeness, Fed.R.Evid. 106. The notes had been used extensively and quoted from copiously by Rubin's counsel on his cross-examination of Cox, possibly leaving a confusing or misleading impression that the portions quoted out of context were typical of the balance. In offering as a "prior consistent statement" the context from which Bender had quoted, the prosecutor was

in reality urging that the entire context would remove the misleading or confusing impression created by the words quoted by Bender, which Rubin might otherwise point to as "illustrative of the whole." Tr. at 879. This amounted to an invocation of the completeness doctrine.

We have repeatedly recognized that where substantial parts of a prior statement are used in cross-examination of a witness, fairness dictates that the balance be received so that the jury will not be misled, *United States* v. *Lev,* 276 F.2d 605, 608 (2d Cir. 1959), *cert. denied,* 363 U.S. 812 (1960); *United States* v. *Weinbren,* 121 F.2d 826, 828-29 (2d Cir. 1941); see generally 7 Wigmore, *supra,* at §§ 2113-2125; Wright & Graham, *supra,* at §§ 5072, 5075, regardless of whether an improper motive existed at or after the prior statement, *see United States* v. *Fayette,* 388 F.2d 728, 733-35 (2d Cir. 1968); *United States* v. *Corrigan,* 168 F.2d 641, 645 (2d Cir. 1948). In this case the context introduced by the prosecutor in the interest of completeness was carefully restricted in scope, being limited to but a few of the 70-odd pages of notes. We are satisfied that these few pages were properly admitted.

Lastly, even if the admission of the excerpts of notes in GX 66A were treated as error, the error would be harmless. The prejudice claimed by Rubin from GX 66A is its use of the word "Pay-off." However, Rubin's counsel had, in his cross-examination of Cox, opened the door when he asked "For example, you have in the notes there [GX 66A] the word 'payoff.' Did Mr. Rubin ever tell any of you that he made a payoff?" Thus the jury was made

aware by Rubin himself that the notes described him as saying that there had been what amounted to a payoff of Ludwig. This was confirmed not only by Cox's testimony but by the balance of the context in which the word was used. Thus the introduction of the notes added little to what the jury already knew.

GX 66B, the agents' one-paragraph note dealing with Rubin's knowledge about the unexecuted contract between Tri-State and Charter Financial, and GX 66D, two pages of notes pertaining to Rubin's participation in the manipulation through Marshall of the OTC pink sheet quotations for All State stock, stand on a somewhat different footing. Prior to their being offered by the Government, there had been no effort by Rubin on cross-examination of Cox to show that they were in any way inconsistent with his direct testimony. They therefore represent prior Cox-adopted statements of what he had been told by Rubin. Rubin's objections to their admission, principally on the ground that no inconsistency had been shown, were rejected. Although these notes are hearsay and if objected to on that ground should not have been admitted, we are satisfied after a careful examination of them that the error was harmless. The substance of GX 66B was peripheral; that in GX 66D was entirely consistent with Cox's detailed testimony on the subject of Rubin's participation in the listing of All States stock in the "pink sheets" by Marshall Murray & Co. Indeed, they even include the statement that "Rubin did not ask Marshall to go into sheet on Allstate." None of the excerpts received in evidence (GX 66A-D), singly or collectively, approximate "a neat condensation of the government's whole case", *United States v. Ware* 247 F.2d 698,

700-701 (7th Cir. 1957), or a detailed summary of the Government's evidence, amounting to "the single most important piece of evidence, testimonial or documentary" against the defendant, *United States v. Quinto supra*, 582 F.2d at 235-36. We can safely say that the few pages of cryptic phrases in this case could not have had any appreciable effect on the jury, in view of the detailed testimony of the Government agents themselves regarding what they were told by Rubin. See *United States v. Ruffin* 575 F.2d 346, 359 (2d Cir. 1978)

Rubin's only other evidentiary claim is that the trial court erred in admitting testimony by Keating that in February, 1973, he was told by Rubin and Deaton that they had applied to a New Jersey bank for a loan that would enable Tri-State to pay its obligations to Bankers Trust but that the New Jersey banker was demanding a bribe. Rubin contends that this testimony was both hearsay and inadmissible as a similar criminal act. *See* Fed.R.Evid. 404(b). We disagree. The statements were admissible as statements made by the conspirators in furtherance of the conspiracy, Fed.R.Evid. 801(d)(2)(E), one objective of which was to lull Bankers Trust into the belief that Tri-State was in good financial condition and would pay its obligation to the bank. Moreover, the New Jersey banker's demand for a bribe did not imply and improper or criminal conduct on Rubin's part.

The Instructions

We find no merit in Rubin's further contention that the trial judge committed reversible error in her instructions to the jury. It was not improper to in-

struct the jury that it is a crime for a banker such as Ludwig or Keating to receive a free gift for procuring a loan, or for one to aid and abet such conduct. This was a correct statement of the law, 18 U.S.C. § 215, and was appropriate in view of Rubin's repeated efforts during the trial to suggest that a banker's receipt of gifts from a borrower was customary and proper, but that the Government was using the threat of criminal prosecution to put pressure on Keating as a witness to testify against Rubin. The court properly advised the jury that it could consider the payments as evidence regarding the means for carrying out the alleged conspiracy and whether Keating had a motive to testify for the Government.

Similarly, the instructions regarding the credibility of witnesses were quite adequate. Since Rubin did not contend that Keating was an accomplice, it was unnecessary to give any instruction to the effect that his testimony must be scrutinized with great care because of such a status. *United States v. Swiderski* 539 F.2d 854, 860 (2d Cir. 1976). Nor did the grant of immunity to Keating require such an instruction in the circumstances of this case. *United States v. Leonard,* 494 F.2d 955 (D.C. Cir. 1974), cited by appellant is distinguishable in that the witnesses testifying under immunity were also accomplices, although no accomplice witness instruction had been requested. The full exploration of immunity on the cross-examination of Keating and in summation, coupled with the trial judge's instruction to the effect that fear of prosecution was a factor to be considered in weighing a witness' testimony was adequate to apprise the jury of any interest adverse to that of Rubin which Keating might have. See *United*

States v. Sarvis, 523 F.2d 1177, 1180-81 (D.C. Cir. 1973) (appeal following retrial after *Leonard)*

The Severance of Rubin

Rubin next argues that it was an abuse of discretion for Judge Motley to have granted the Government's motion to sever Rubin from his co-defendants and to try him separately. We disagree. Although a severance at the Government's insistence is probably a rarity—usually it is the defendant who seeks such relief—it is permissible under the language of F.R. Crim.P. 14 which provides in relevant part that "[i]f it appears that . . . the government is prejudiced by a joinder of . . . defendants in an indictment . . . or by such joinder for trial together, the court may . . . grant a severance of defendants or provide whatever other relief justice requires." Although it is true that "[a]s a general rule persons jointly accused should be tried in a single trial, particularly where the charges may be proved against all the defendants by substantially the same evidence, or are based upon the same or a similar series of acts," *United States v. Zim Israel Navigation Co.*, 239 F. Supp. 446, (S.D.N.Y. 1965) (Weinfeld, *J.*), "[i]t [is] within the sound discretion of the trial judge as to whether the defendants should be tried together or severally . . . ." *Opper v. United States*, 348 U.S. 84, 95 (1954).

The basis for the Government's motion was its plan to introduce against Rubin admissions he made during the interviews with the federal agents, which would create potential problems under *Bruton v. United States*, 391 U.S. 123 (1968), with respect to other defendants. The interview notes contained a great deal of detail regarding the conduct of Rubin's

co-defendants. Rubin's defense depended heavily on his argument that although he committed certain acts he did so innocently, and that those who were giving him instructions were the ones with the corrupt motives. The likelihood that Rubin's co-defendants would have invoked their Fifth Amendment privilege at a joint trial, the inability of the Government or the court to ascertain at the time of the motion whether Rubin would take the stand in his own defense, demonstrate that the trial judge acted well within her discretion in granting a severance. *See Garris v. United States,* 418 F.2d 467, 470, n.6 (D.C. Cir. 1969); *United States v. Dioguardi,* 20 F.R.D. 10, 14 (S.D.N.Y. 1956). This case is an appropriate one for application of the principle that "[n]o accused person has any recognizable legal interest in being tried with another, accused with him, though he often has an interest in not being so tried." *United States v. Bronson,* 145 F.2d 939, 943 (2d Cir. 1944) (L. Hand, *J.*). *See United States v. Marchant,* 25 U.S. (12 Wheat.) 480, 482-83 (1827); *United States v. Arcuri,* 405 F.2d 691, 695 (2d Cir. 1968), *cert. denied,* 395 U.S. 913 (1969). In view of the cogent reasons for a separate trial, the balance weighed heavily in favor of granting the Government's motion.

Statute of Limitations and Pre-Indictment Delay

Rubin's next contentions—that the indictment, which was filed on January 27, 1978, should have been dismissed as barred by the five-year statute of limitations, 18 U.S.C. § 3282, and because of unreasonable pre-indictment delay, require little discussion. The former claim is based on the er-

roneous premise that the conspiracy terminated on December 6, 1972, when the last of the fraudulently-obtained loans were turned over by Bankers Trust to Tri-State, or at least on January 19, 1973, when the last collateral was pledged. This misconceives the scope of the alleged conspiracy, which was to continue the scheme of fraudulently obtaining loans and lulling lenders into not calling them. Toward this end Rubin, Deaton and James in January and February 1973 attempted to borrow funds from others, misrepresented to Ludwig and Keating Tri-State's financial condition and the value of the pledged collateral, and falsely listed the All States stock in the OTC pink sheets, with the result that on February 26, 1973, James executed a consolidated rollover demand note, falsely representing to Keating that a railroad strike had hampered coal deliveries. This overt act was clearly in furtherance of the conspiracy and not a mere coverup or concealment of a completed scheme. See *Grunewald v. United States,* 353 U.S. 391, 405-06 (1957); *United States v. Knuckles,* 581 F.2d 305, 313 (2d Cir. 1978); *United States v. Floyd,* 555 F.2d 45, 48 (2d Cir.), *cert. denied,* 434 U.S. 851 (1977); *United States v. Frank,* 494 F.2d 145, 155-56 (2d Cir.), *cert. denied,* 419 U.S. 828 (1974).

To establish denial of due process based on excessive pre-indictment delay Rubin bears the heavy burden, for the reasons stated by the Supreme Court in *United States v. Lovasco,* 431 U.S. 783 (1977), of showing not only that he was prejudiced by the delay but that it was so unfair as to violate fundamental concepts of fair play and decency, such as would occur if the prosecutor deliberately used the

delay to achieve a substantial tactical advantage. 431 U.S. at 790, 795. The statute of limitations still provides "the primary guarantee against bringing overly stale criminal charges," *United States v. Marion*, 404 U.S. 307, 322 (1971); *see also United States v. Eucker*, 532 F.2d 249, 255 (2d Cir.), *cert. denied*, 429 U.S. 822 (1976).

No such showing has been made here. After a thorough hearing Judge Motley found that the delay had not been "due to any [Government] attempt to gain a tactical advantage" and that Rubin had failed to demonstrate actual prejudice. We find no grounds for disturbing these findings. The pre-indictment delay was justified in large measure for several reasons, including the complexity of the evidence, the pendency of an extensive investigation into tax evasion charges, which then had to be dropped for venue reasons, and the resulting interviews of many witnesses from different parts of the country, coupled with an analysis of voluminous financial records, which led to the indictment on non-tax counts. The prosecutor was justified in not seeking the indictment until she was convinced that there would be sufficient evidence to prove guilt beyond a reasonable doubt. Moreover, prior to indictment the prospective defendant suffers no restraint on his liberty. In any event our review of the record fails to reveal any actual prejudice of the type that is legally cognizable. Faded recollections and missing peripheral witnesses are not enough, *United States v. Vispi*, 545 F.2d 328, 331-332 (2d Cir. 1976).

We have examined each of the other points raised by Rubin and find them to be without merit.

The judgment of conviction is affirmed.

FRIENDLY, *Circuit Judge,* concurring:

Although Judge Mansfield's opinion thoroughly demonstrates that Rubin's conviction should be affirmed even if the limitations of Federal Rule of Evidence 801(d)(1)(B) applied in terms when a prior consistent statement was offered only for rehabilitation, it seems to me important for the future to make clear that despite the contrary dictum in *United States v. Quinto,* 582 F.2d 224, 233-34 (2 Cir. 1978), see also *United States v. Check,* 582 F.2d 668, 681 n. 40 (2 Cir. 1978), the limitations apply only to the use of prior consistent statements as *affirmative evidence* and are not controlling when such statements are used *only for rehabilitation.* Some background is needed to illuminate the problem.

Before adoption of the Federal Rules of Evidence, there had been a lively controversy summarized in 4 Wigmore, Evidence, § 1126 (Chadbourn rev. 1972), over the use of prior consistent statements to rehabilitate a witness whose credibility had been attacked on the basis of a prior inconsistent statement. There had been little need to consider the use of prior consistent statements as affirmative evidence, since they were no more probative for that purpose than what the witness had said or could say on the stand; indeed, the case law was practically unanimous in rejecting the use of prior consistent statements as affirmative evidence although the Uniform Rule of Evidence 63, adopted in a few jurisdictions, was to the contrary. See 4 Wigmore, *supra,* §§ 1124, 1132. On the point that was in controversy, namely, the use of prior consistent statements for rehabilitation after impeachment by an inconsistent

statement, a number of views had emerged. Two of these, both rather simplistic, were a minority view "that if a contradictory statement counts against the witness, a consistent one should count for him", and a majority view that "since the self-contradiction is conceded, it remains as a damaging fact, and is in no sense explained away by the consistent statement." *Id.* at 259. However, adherents of the majority view recognized an exception when the making of the prior consistent statement would tend to dispel a charge of recent fabrication or improper motive. See Note, Evidence of Prior Consistent Statements Admissible for Rehabilitation when Witness' Testimony Assailed as Recent Fabrication, 45 Calif. L. Rev. 202 (1957).

A third view, apparently originating in Judge Cooley's opinion in *Stewart v. People,* 23 Mich. 63, 74-76 (1871), rightly considered the problem to be more complex and not susceptible to any bright-line solution. Judge Cooley pointed to a number of situations beyond those of recent fabrication and improper motive where it would outrage common sense to reject the prior consistent statement for rehabilitation. The clearest case was when the making of the inconsistent statement was disputed. Thus, when a person was "testifying in a case where he had spent a considerable period of time and a large sum of money in pursuing an alleged criminal to conviction, and he is confronted with evidence of his own conflicting statements," he should be entitled to demonstrate "such circumstances of his connection with the case as would make the impeaching evidence appear to be at war with all the probabilities." Beyond these, "other cases may readily be supposed in which,

under the peculiar circumstances, the fact that the witness has always previously given a consistent account of the transaction in question might well be accepted by the jury as almost conclusive that he had not varied from it in the single instance testified to for the purpose of impeachment." He concluded that "though such evidence should not generally be received," its admission "ought not to be set aside except in a clear case of abuse" of discretion.

The most cited decision on the subject in this circuit was Judge Learned Hand's opinion in *United States v. Sherman,* 171 F.2d 619, 621-22 (1948), *cert. denied sub nom. Grimaldi v. United States,* 337 U.S. 931 (1949). In that case, a prosecution for stealing goods in interstate commerce, one Oliva testified that Sherman not only was a party to the theft but drove the truck used to effectuate it. The defense impeached Oliva with a written post-arrest statement in which he had not mentioned Sherman and had identified one Whelan as the driver of the truck, and the trial court then allowed the prosecution to introduce a second written statement, made a few weeks after the first, which coincided with the trial testimony. In reversing, Judge Hand said this:

> Concededly the second statement was not competent unless the admission of the impeaching statement made it so, for when Oliva made it he had the same motive to fabricate—the hope of lenity—that he had while on the stand. Rationally, it is true, the fact that he changed his story so soon after making the contradictory statement, may have added to the persuasiveness of his testimony; and for that matter most persons would probably consider any earlier consistent

> account, in some measure at least, confirmatory of a witness's testimony. The reason for its exclusion is because it has not been made on oath rather than because it has no probative value, although courts have often spoken as though it had none. However, such a statement is as incompetent when the witness has been impeached by an inconsistent statement, as when he has not been. So the Supreme Court decided many years ago; and although the point has apparently never come up again in that court, the lower federal courts have several times applied or recognized the doctrine. (footnotes omitted)

With all respect, the analysis is hard to follow. Judge Hand clearly rejected the irrelevancy argument which was the cornerstone of the majority view. His reason for excluding the evidence was rather that it had "not been made on oath," which sounds in hearsay although he did not add "and subject to cross-examination." But Oliva's second statement was *not* hearsay since, apart from other considerations, it was not offered as proof of the matter asserted but only because the very fact of its having been made would "break the force of the impeachment".

Only two years later this court rendered a decision fundamentally inconsistent with Judge L. Hand's hearsay theory. In *United States v. Corry*, 183 F.2d 155, 156-57 (1950), the court, speaking through Judge A. N. Hand and following Judge Cooley, approved the sensible action of then District Judge J. Joseph Smith in allowing the jury to consider prior consistent statements by government witnesses, without any limitation on the score of difference in

motivation, where there was an issue whether an alleged inconsistent statement had been made. We regularly permitted use of consistent statements for rehabilitation without the need of any further showing when, as here, they were needed in the interest of completeness, see *United States v. Weinbren,* 121 F.2d 826, 828-29 (2 Cir. 1941); *United States v. Lev,* 276 F.2d 605, 608 (2 Cir.), *cert. denied,* 363 U.S. 812 (1960); *United States v. Fayette,* 388 F.2d 728, 733-35 (2 Cir. 1968) (Medina, J.). Later in *Felice v. Long Island Railroad Co.,* 426 F.2d 192, 197-98 (2 Cir.), *cert. denied* 400 U.S. 820 (1970), we again approved Judge Cooley's approach, recognizing the peculiar appropriateness of admitting prior statements, quite apart from a claim of recent fabrication, in order to explain away a claim of incompleteness in a statement used in impeachment, and said that "a good deal of latitude should be accorded trial judges in admitting prior consistent statements for rehabilitation." Shortly thereafter, in *Applebaum v. American Export Isbrandtsen Lines,* 472 F.2d 56, 60-62 (1972), the court, speaking through Judge Mansfield, reversed a judgment because of the exclusion of a prior consistent statement offered for rehabilitation in the face of a later inconsistent statement, even though there was nothing to indicate any difference of motivation on the two occasions. This court's flexible approach to the use of prior consistent statements for rehabilitation, with an appropriate limiting charge to be given if requested, was the rule generally followed in the federal courts when the Federal Rules of Evidence were being framed. *Affronti v. United States,* 145 F.2d 3, 7-8 (8 Cir. 1944) (Sanborn, J.) (if some portions of a statement

are used for impeachment, other relevant portions may be used to meet its force); *Cafasso v. Pennsylvania R. Co.*, 169 F.2d 451, 453-54 (3 Cir. 1948) (Maris, J.). See also McCormick, Evidence § 49 at 106 (Cleary ed. 1972).[1]

Since the only mention of prior consistent statements in the Federal Rules of Evidence is in Rule 801(d)(1)(B) and this limits admission to cases where the statement "is offered to rebut an express or implied charge against him of recent fabrication or improper influence," lawyers and judges can be forgiven for being misled into concluding, as was done by dictum in *United States v. Quinto, supra,*[2] that the

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1 The decisions of this court in *United States v. Lombardi*, 429 F.2d 216, 220 (1970) and *United States v. Zito*, 467 F.2d 1401, 1403-04 (1972), approving the admission of prior consistent statements for rehabilitation to rebut a charge of recent fabrication in no way show that this was the only instance in which such use was permissible. As indicated, in several cases we had gone beyond this.

2 The statement in *Quinto* with respect to rehabilitation was no less dictum because the opinion characterized it as a holding. As the *Quinto* opinion clearly showed, the trial court had received the agents' memorandum as direct evidence "under 801(d)(1)(2) [sic]," see 582 F.2d at 231-32, which provides for admission for the truth of the matter asserted. This court held such admission to constitute error under that provision. Anyone reading the opinion can readily see that this was the only issue presented; nothing in the opinion suggested that questions had been raised whether the memorandum could be used solely for rehabilitation if that issue were to arise on a new trial and the briefs show that none had been. It is particularly puzzling that Judge Meskill should regard ourselves as bound by the unnecessary statement in *Quinto* with respect to rehabilitation when, as he correctly says, the Federal Rules of Evidence have not changed the law governing admission of prior consistent statements for that purpose which was considerably broader than Rule 810(d)(1)(B). A judge's power to bind is limited to the issue that is before him; he cannot transmute dictum into decision by waving a wand and uttering the word "hold". There should hardly be need to recall the long established Supreme Court jurisprudence

limitation applies to the use of prior consistent statements for rehabilitation as well as for direct evidence. However, analysis makes it clear that Rule 801(d)(1)(B) simply does not deal with the extent to which prior consistent statements may be used for rehabilitation.

The cited provision is in a definitional section of the article of the Rules which deals with hearsay; Rule 801(d) says that certain consistent statements, among them consistent statements of the kind there enumerated, are not hearsay. But, *pace* Judge Learned Hand's statement in *Sherman,* consistent statements used *only* for rehabilitation are never hearsay since they are not "offered in evidence to prove the truth of the matter asserted", Rule 801(c), but only for the fact of their having been made, 4 Wigmore, *supra,* § 1132 at 294 and cases there cited in n. 1. By allowing *certain* prior consistent state-

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that, as said in *Cohens v. Virginia,* 6 Wheat. (19 U.S.) 264, 399-400 (1821):

> It is a maxim, not to be disregarded, that general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit, when the very point is presented for decision. The reason of this maxim is obvious. The question actually before the court is investigated with care, and considered in its full extent. Other principles which may serve to illustrate it, are considered in their relation to the case decided, but their possible bearing on all other cases is seldom completely investigated.

So far as concerns *United States v. Check,* 582 F.2d 668, 680-81 (2 Cir. 1978), the text of the opinion, written by the distinguished author of *Quinto* and filed only three weeks earlier, carefully and properly limited the effect of Rule 801(d)(1)(B) to the use of consistent statements as affirmative evidence, again the only point there at issue, although note 40 volunteered that "the statements were not admissible even for the more limited purpose of bolstering the witness' credibility."

ments to be used as proof of the matter asserted, as they could not previously have been, Rule 801(d)(1)(B) does not imply that others not meeting that standard can never be used for rehabilitation. The Note of the Advisory Committee reproduced in the margin[3] makes clear that the purpose of Rule 801(d)(1)(B) was to admit for general use a category of prior consistent statements that "traditionally" had been admissible for rehabilitation. It does not at all follow, as was said in *Quinto, supra,* 582 F.2d at 233, without benefit of briefing, that the exemption of only certain consistent statements from exclusion as hearsay also determines "which varieties of prior consistent statements can be admitted for the more limited purpose of rehabilitation." Apart from the fact that an article of the Rules concerned with hearsay would be a strange place for dealing with rehabilitation, the very fact that the latter is a "more limited purpose" would suggest that the standard should *not* be so rigorous. What other types of consistent statements might be received for rehabilitation is a subject, like many others, to which the Rules do not speak.[4] Judge Weinstein's treatise

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3 Prior consistent statements traditionally have been admissible to rebut charges of recent fabrication or improper influence or motive but not as substantive evidence. The prior statement is consistent with the testimony given on the stand, and, if the opposite party wishes to open the door for its admission in evidence, no sound reason is apparent why it should not be received generally.

4 It is not entirely clear why the Advisory Committee felt it necessary to provide for admissibility of certain prior consistent statements as affirmative evidence. As indicated above, this had been a non-problem. Evidently the Committee considered that since it was permitting certain types of inconsistent statements to be admitted as proof of the facts stated, Rule 801(d)(1)(A), in line with our decision in *United States v. DeSisto,* 329 F.2d 929, *cert. denied,* 377 U.S. 979 (1964), it ought to confer a similar benefit on some consistent statements.

attests that the purpose of Rule 801(d)(1)(B) was simply to give substantive effect to prior consistent statements meeting its standards, 4 Weinstein's Evidence, ¶ 801(d)(1)(B)[01] at 801-99 (1978), thereby moving part but not all of the way toward Uniform Rule of Evidence 63. To apply the severe limitations of Rule 801(d)(1)(B) as a universal rule restricting the use of prior consistent statements for rehabilitation is thus unjustified as a matter of language and of history, and would run counter to the instruction of Rule 102 that:

> These rules shall be construed to secure fairness in administration, elimination of unjustifiable expense and delay, the promotion of growth and development of the law of evidence to the end that the truth may be ascertained and proceedings justly determined.

Liberality in allowing prior consistent statements for rehabilitation is peculiarly demanded when, as here, a court is dealing with a record of what was said as distinguished from a narrative of what occurred. The fact to be proved by Agent Cox' testimony was not what Rubin had done but what he had said in his interviews by the agents, Rule 801(d)(2). The allegedly inconsistent and consistent statements were all in one set of records, made at substantially the same time. Under such circumstances, a court that has received inconsistent statements in such records for impeachment should be generous in allowing consistent ones for rehabilitation, since they bear on whether, looking at the whole picture, there was any real inconsistency. This is the great principle of completeness, now enacted

in Rule 106. The important thing is that, unless the prior consistent statements are admissible as affirmative evidence under Rule 801(d)(1)(B), the jury should be clearly apprised, if requested, that they are to be considered solely as breaking the force of the impeachment.

MESKILL, *Circuit Judge*, dissenting:

I respectfully dissent. Although I agree with the majority that neither the pre-indictment delay nor the statute of limitations requires dismissal of the indictment against Rubin, and that the severance of Rubin's trial from that of his co-defendants was not an abuse of discretion, I dissent from the view that the judgment of conviction should be affirmed. The unusual circumstances of Rubin's trial which I believe require reversal and a new trial deserve review in considerable detail.

Between July of 1973 and July of 1976 Rubin was interviewed by government agents and attorneys, including Internal Revenue Service Agent Thomas Cox, several times. Rubin was told of the nature of the government investigation, was advised to obtain counsel, and was asked to consider cooperating. He was also told that "the Government was not going to let him walk away." No written statement was taken from Rubin, but the agents took extensive notes during their interviews. These notes totalled more than 70 pages and were marked Government Exhibit (GX) 66 for identification. Although Cox himself took none of the notes, he testified that he reviewed the notes at the close of each session and believed that they accurately reflected the interviews. Rubin was

never shown the notes; nor was he asked to sign them as accurately reflecting the interview; nor were they signed by the agent who had written them. Some of the notes were handwritten and some were typed.

Cox took the stand early in the trial. He said he had been present at approximately twelve of the Rubin interviews. He at first had some difficulty remembering when he began attending the sessions with Rubin, saying once "around January 1973" and another time "something like October '73." Asked if there were any documents that would help him be more specific, he said the notes of the interviews might help him. Using GX66 to refresh his recollection, he said that January 9, 1974, appeared to be the date being sought. Louis Bender, Rubin's attorney, objected that Cox was reading the notes rather than refreshing his recollection, and Cox was instructed to use the notes only to refresh his recollection. Cox then proceeded to testify as to what he remembered Rubin saying during the interviews he attended. He constantly was reminded to use the notes only for the refreshment of his recollection.

On cross-examination, Bender began to use the notes to challenge Cox's recollection of what Rubin had said during the interviews. Bender wanted to show that although Cox had testified that Rubin had said certain things during the interviews, the notes of the interviews did not bear him out. The government then suggested that Bender should offer the notes into evidence, a suggestion Bender characterized as "unnecessary" and "self-serving." The court, too, said that "if we are going to read from the notes and ask the witness to read from them, they

should be in evidence." Bender then explained that he was treating the notes "like a prior statement made by an agent who was present" and that he had a right "to read a prior inconsistent statement, if it is." The court then made the following ruling:

> THE COURT: It isn't his statement. He said that he did not write those notes. He said that somebody else made that memorand[um]. He used it to refresh his recollection. So you can't use that to impeach his credibility. You can use any statement which he made or any report which he made in writing to impeach his credibility. When somebody else has made the notes you can't attribute it to him.

Bender and the court then made the following agreement—Bender could use the notes to challenge Cox's earlier testimony where he could show that Cox had relied on the notes instead of his independent recollection, but Bender could not use the notes to impeach Cox's credibility.[1] Cox was on the stand for the better part of two days, going through direct examination, cross-examination, redirect and recross.

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1 Compare Fed. R. Evid. 612, which provides in part:

> Except as otherwise provided in criminal proceedings by section 3500 of title 18, United States Code, if a witness uses a writing to refresh his memory for the purpose of testifying, either—
>
> (1) while testifying, or
>
> (2) before testifying, if the court in its discretion determines it is necessary in the interests of justice,
>
> an adverse party is entitled to have the writing produced at the hearing, to inspect it, to cross-examine the witness thereon, and to introduce in evidence those portions which relate to the testimony of the witness.

See also note 9, *infra*.

At least for purposes of this dissent, the most important portion of his testimony is that which follows.

Cox testified on direct as to what Rubin had told the agents about the meetings he had had concerning the approval of the requested loans. For example, Cox said that Deaton, Rubin and James went to the bank with the prepared financial statement, had the loan approved, and then had a discussion afterwards about their success. Cox testified that Rubin had told the agents that this discussion included the following:

> COX: Deaton said that Ludwig had to be taken care of.
>
> And he asked Rubin how much should he give him. And Rubin said, "I don't know. I've never paid off before." And Deaton said, "Well, what about 5 percent?" And he said, "That should keep Ludwig happy."

On cross-examination, the following exchange took place:

> BENDER: Because you are trained people, you put down your own thoughts on what you pick up from outsiders on notes when you are interrogating a witness? For example, you have in the notes there the word "payoff." Did Mr. Rubin ever tell any of you that he made a payoff?
>
> COX: Using those two words together, he didn't —actually, that he said "payoff"? I can't say he used that expression.
>
> BENDER: He said he gave money to Mr. Ludwig and he gave money to Mr. Keating, isn't that right?
>
> COX: That's right.

BENDER: Did Mr. Rubin ever tell you that he used the word in talking with you, "bribe"?

COX: I can't say he used the word "bribe" either, no.[2]

On redirect, the government offered pages 1 and 2 of the handwritten notes from the interview dated October 10, 1974, as a "prior consistent statement" by Cox, that is, as a prior statement by Cox relating to Rubin's statements during the October 10 interview regarding payments. The government offered these notes under this theory despite the trial court's earlier ruling that Bender could not treat the notes as prior statements by Cox for purposes of impeachment, the apparent theory being that Bender had used the notes as "prior inconsistent statements" by Cox, that Cox had "adopted" the notes as his own statements, and that because of the nature of the cross-examination the government was entitled to put in Cox's "prior consistent statements." The exhibit was marked GX66A; the text of GX66A is set out in the margin.[3]

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2 Earlier in the cross-examination of Cox, Cox had said to Bender that he did not have to rely on the notes in order to recall the "bribe," meaning the payment of money by Rubin to Ludwig. Bender immediately asked that the answer be struck, explaining that Rubin had not used that term in his interview. At this point the government attorney said that if Bender were to ask Cox if the words "paid off" and "bribe" were Rubin's or his, that Cox would say they were Rubin's. The court suggested that Bender ask precisely that question, but Bender said he did not want to ask it because "that's like putting my head in the lion's mouth." The court then told the jury that they were the ones who would have to decide whether the payments to Ludwig were bribes.

3 *GX66A*

[October 10, 1974
Pages 1 & 2
Attended by Rubin and Ruffa (Rubin's lawyer) and Levitt, DeGroot, Uberall and Cox (of the government) ***handwritten***] .

Bender immediately objected:

BENDER: Your Honor, in view of the fact that Mr. Cox has indicated that some of the notations

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Pay-off
Day L. approved loan (10-20-72)
as per bk. [or "after bk."]
In st. (R&D)—conv.
cont'd—in office W. J.
Street D—wants to know—how much
$ for L?
R—Don't know—never pd. off
D—Asks if 5% wld. be o.k.
R—Don't know.
D—We'll discuss with J.
when back in office. But we
better take care of L. on Monday.
D & L tell J. abt. L.
Discussion—what to pay "L"
D—Expect [or "Exper."]—5% to bankers.
R—Rumors L "on take"
J—Give L something
D—Only 1500 avail. from
proceeds after budgeting
L will be satisfied & will
owe balance to him.
Tells R—You know L best
—You give money. Tell
him there will be more.
Deaton draws ck. to cash ($1500
Endorses.
D—Wants R to cash at bank
R—Thought too risky.
R—Will cash at Englewood
CC over wkend.
R cashes over wk'nd.
RD&J
Monday morning in office
R—Have money do you
want to turn over now
or shld we wait—might
be cash short.
D—Instructed to take cash
to L. & put in envelope
Coffee shop episode—O.K.
R tells L—more coming.
R then goes to office
& tells D & J money delivered.
D&J—L happy?
R—Told L more coming &
L seemed to be pleased.

which appear in these notes are notations which were written without any relationship, or that is, were written not from what Mr. Rubin said but their own characterizations, I cannot see how this could be a memorandum of a recollection past recorded as to what Mr. Rubin said to them. Certainly it doesn't have any credibility, at least as far as this case is concerned, what an agent may characterize something to be, rather than what Mr. Rubin himself is reflected as having been said.

So that actually these notes really do not reflect what the agents state Mr. Rubin said and, for that reason, it's objectionable.

I have no objection to Miss Neugarten going in and asking him any question that I did about the notes and see if it refreshes his recollection; but to put this in evidence as if statements which appear here in this paper come from Mr. Rubin, when this witness said they have not, would be, I think, objectionable.

NEUGARTEN: Your Honor, the witness had indicated that he "adopted the statement," by reviewing the notes soon after they were taken, believing them to be accurate.

The witness has been cross-examined as to allegedly prior inconsistent statements concerning what Mr. Rubin said.

Given that, I believe that there has been an implied or expressed challenge, either to the witness' recollection or his credibility, and that as a result I am allowed to permit prior consistent statements.

The court then inquired as to the inconsistency that the government was hoping to clear up by the intro-introduction of the notes, the assumption apparently being that if the government could point to an inconsistency in Cox's testimony that Bender had uncovered during cross then the government would be allowed to introduce the notes as Cox's prior consistent statements. The government responded as follows:

> NEUGARTEN: Your Honor, two specific inconsistencies have been drawn to the witness' attention. I believe Mr. Bender's attack has been to go to peripheral matters and attempt to find inconsistencies, and then he will argue to the jury that they are illustrative of the whole.
>
> He has stayed away like a scared rabbit from the central core, the payments where, of course, the witness has been consistent all the time. But then he has set himself up to argue that something inconsistent as to one thing is inconsistent as to everything.
>
> I think there is such explicit detail on payment here that the jury should be allowed to see the consistency of the prior statement.

Bender objected that the word "payoff" was the word used by the agent who had written the notes and not the word used by Rubin in the interview.

> BENDER: Judge, you see he [Cox] has testified that this word is their word, not Rubin's. He has already testified to this in detail, what appears on this first page. But to put this in, your Honor, after he has already testified to it, is to

give a semblance of belief that Mr. Rubin actually used the word "payoff," just like we said that it was the agents that wrote the notes, that wrote "bribe," that Mr. Rubin never used that word.

So this is just an attempt by the government to get this man's testimony which he has already given as to what Rubin said before the jury, by having these notes here.

To this the court responded:

THE COURT: It is true that on direct, [Cox] said "payoff." On cross, he said he didn't remember those were his exact words. Now [the government] is going to put this in, to show that that was what he put down initially.

When the government suggested further that the "on take" quotation in the notes was what Rubin had actually said during the interview, Bender again argued that that was what the agent had written down rather than what Rubin had actually said. Bender then argued that the agent who had written the notes, rather than Cox, should be the one to say that the notes were statements of what Rubin had said at the interviews.[4] All of his objections were

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4 During its rebuttal case, the government called Edward J. Levitt, a special attorney with the Department of Justice Criminal Division. He testified on direct that he was the person who wrote the notes now known as GX66A. He said that when he took notes during interviews he would put quotation marks around "key words:"

Whenever there were what I felt were key words, somebody relating them to me, what I would do is put them down and quote them, that is make quotes around the words meaning

overruled, and the excerpt was admitted into evidence; Cox then recited it orally to the jury.

As explained in the majority opinion, the notes labeled GX66A were not the only ones introduced by the government in this fashion.[5] As also explained by the majority, Bender himself was on occasion able to take advantage of the existence of the notes.[6] The jury asked to see the notes during the course of their deliberations.

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those were the words that the person used in describing to me what had occurred.

Thus, the phrase "on take" is quoted in the notes, indicating that Levitt believed Rubin used that phrase to describe what he had heard about Ludwig. The phrase "paid off" is not in quotation marks. On cross-examination, Levitt testified that Rubin did *not* use the term "pay off" during the October 10, 1974, interview:

The answer is at that occasion I do not think he used the term "pay off," I believe I used the term "pay off."

On redirect, Levitt testified that Rubin had used neither the term "pay off" nor the phrase "paid off" during the October 10 interview, and that those terms were his (Levitt's) characterization of what Rubin had said. He did say, however, that Rubin had used the phrase "paid off" on a prior occasion, July 19, 1973. My inspection of the notes that appear to be dated July 19, 1973, reveals the following entry: "Keating and Ludwig paid off by Rubin.—c.$4 m." The phrase "paid off" is not in quotes.

5 For example, GX66B, relating to the Charter Financial asset included in the financial statement submitted to the bank, was offered by the government "as a prior consistent statement of the witness," Agent Cox, the express purpose for which was "to show Mr. Rubin's state of mind" as it related to the question whether he knew that the Charter Financial contract had never been executed. Similarly, GX66C, relating to the imprisonment of Raymond Starns, was offered by the government "as a prior consistent statement of the witness," against Agent Cox. And GX66D, relating to Rubin's purchase of All States stock and its listing in the "pink sheets," was introduced by the government "as a prior consistent statement on the subject of pink sheets."

6 For example, on direct Cox testified that at the January 9 interview Rubin had described the initial contacts between Tri-State (represented by Deaton and Rubin) and Bankers Trust

On appeal, Rubin argues that the "erroneous admission of pre-trial interview notes as prior consistent statements of Government witness Special Agent Thomas Cox" requires reversal of the judgment of conviction, Brief at 12, citing as authority this Court's decisions in *United States v. Check,* 582 F.2d 668 (2d Cir. 1978), and *United States v. Quinto,* 582 F.2d 224 (2d Cir. 1978). Because the text of some of these notes dealt with the payments made by Rubin to Ludwig and Keating, described by the government as the "central core" of its case, and because Rubin's main defense was that although he made the payments they were considered by him to be after the fact tokens of appreciation rather than "bribes" or "pay offs," Rubin argues further that the error was harmful. For the reasons that follow, I agree with both contentions.

The first question, of course, is whether Rubin's trial counsel objected in such a way as to allow him to raise this issue on appeal. The relevant rule, Fed. R. Evid. 103(a)(1), provides:

(represented by Ludwig and Keating) regarding the possibility of loans to keep Tri-State afloat. Cox said that Rubin had said at the interview that, after the meeting, Rubin had said to Ludwig, "Look, Ray, if you can see your way clear to help us, we will take care of you." On cross, Bender pointed out that the notes included in quotes the sentence, "If you take care of us we will take care of you," but that immediately after this quotation was the notation, not in quotes, "No—Don't No." Cox did not remember Rubin's making this latter statement. This testimony was, understandably, viewed by both the government and defense counsel as relevant to Rubin's knowledge and intent with regard to the making of payments to Ludwig and Keating.

Subsequently, Agent Jennings, also present at the January 9 meeting, testified that Rubin had said that *Deaton* had made the "Look, Ray . . . ." comment, and then had told him (Rubin) about it later.

> Error may not be predicated upon a ruling which admits or excludes evidence unless a substantial right of the party is affected, and . . . [i]n case the ruling is one admitting evidence, a timely objection or motion to strike appears of record, stating the specific ground of objection, if the specific ground was not apparent from the context.

This Court has on a number of occasions referred to the importance of this rule and the strictness with which it should ordinarily be applied. But if we have learned anything in our deliberations, it is that reciting the rule is much easier than applying it: "The dividing line between specific and general objections is only clear at the extremes . . . . In between . . . are a lot of good faith, though fumbling, efforts to communicate objections . . . ." 21 Wright & Graham, Federal Practice and Procedure: Evidence § 5036, at 183. In my judgment, the objections put forth by Rubin's attorney were, under the circumstances, sufficient to justify reaching the merits of this portion of the appeal.

After rejecting as "self-serving" the government's suggestion during cross-examination that he be the one to introduce the interview notes into evidence, Bender himself tried to justify the reading of portions of the notes as a device to challenge Cox's credibility be means of prior inconsistent statements. But, as noted above, the court rejected his efforts:

> THE COURT: It isn't his statement. He said that he did not write those notes. He said that somebody else made that memorand[um]. He used it to refresh his recollection. So you can't use that

> to impeach his credibility. You can use any statement which he made or any report which he made in writing to impeach his credibility. When somebody else has made the notes you can't attribute it to him.

When on redirect the government, the district court's earlier ruling notwithstanding, offered the notes on the precise and express ground that they were "prior consistent statements" by Agent Cox, Bender, knowing that Cox himself had not written the notes, no doubt assumed that the trial court would reject them on the same basis as was stated in the prior ruling. But this was not to be. Bender then objected that Cox had admitted on cross that the notes included characterizations by the agents of the gist of what Rubin had said rather than statements of Rubin's actual words; that the notes could not be admitted as a memorandum of past recollection recorded (a well known exception to the hearsay rule);[7] and that the agent who had actually written the notes should be the one to state that the notes were accurate statements of what Rubin had said during the interviews, not an agent who was merely present and had not written the notes. At other points, Bender argued

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7 Fed. R. Evid. 803 provides:

> The following are not excluded by the hearsay rule, even though the declarant is available as a witness:
>
> . . . .
>
> (5) Recorded recollection. A memorandum or record concerning a matter about which a witness once had knowledge but now has insufficient recollection to enable him to testify fully and accurately, shown to have been made or adopted by the witness when the matter was fresh in his memory and to reflect that knowledge correctly. If admitted, the memorandum or record may be read into evidence but may not itself be received as an exhibit unless offered by an adverse party.

that what were being offered as "prior consistent statements" by Cox should not be admitted in the absence of some inconsistency that had been developed on cross between Cox's testimony on direct and the contents of the notes.

When evidence is offered expressly under the rubric of "prior consistent statement," and when an objection to that offer is made, the obvious question presented is whether the evidence is admissible as a prior consistent statement. Bender had good reason to assume that it could not be so admitted, given the trial court's prior ruling on that precise issue. Bender's objection that the notes could not be admitted as past recollection recorded also should have made it clear that in the absence of an applicable exception the proffered evidence was inadmissible hearsay. Given this "context," Fed. R. Evid. 103(a)(1), I would choose to reach the merits. *See also* Fed. R. Evid. 102:

> These rules shall be construed to secure fairness in administration . . . and promotion of growth and development of the law of evidence to the end that the truth may be ascertained and proceedings justly determined.

I note first that, in my judgment, we are limited on this appeal to the question whether the interview notes were properly admitted as prior consistent statements by Agent Cox. As explained in *United States v. Check, supra,* 582 F.2d at 683, "it would be unfair to consider the admissibility of the evidence for any narrower purpose than that upon which the testimony was unquestionably offered and received at trial." *See also id.* at 681-82, *quoting*

Shepard v. United States, 290 U.S. 96, 102-03 (1933). Accordingly, I would refrain from resolving the questions raised on this appeal by reference to the so-called doctrine of completeness. Fed. R. Evid. 106 provides:

> When a writing or recorded statement or part thereof is introduced by a party, an adverse party may require him at that time to introduce any other part or any other writing or recorded statement which ought in fairness to be considered contemporaneously with it.

Even assuming that the notes were "introduced" by Bender for purposes of the rule because he "utilized [them] in court," *see* Wright & Graham, Federal Practice and Procedure: Evidence § 5075, and assuming that this served to render otherwise inadmissible evidence admissible, *compare* Weinstein & Berger, Weinstein's Evidence ¶ 106[01], at 106-12, *with* Wright & Graham, *supra*, § 5072, at 346, it is my belief that this Court should not go about concocting theories to support the otherwise erroneous admission of evidence. The rule itself provides that the party seeking its benefits is obliged to invoke its provisions. "Like other evidence rules, the completeness doctrine does not automatically apply; it must be invoked by a party." Wright & Graham, *supra*, § 5076, at 360. Here, to affirm the introduction of these interview notes by citing Rule 106 would be to apply the rule not only "automatically" but retroactively as well. This I would decline to do.[8] And even if I were

8 I note a certain irony in this regard—if on this record it can be said that the government invoked Rule 106, then surely it can also be said that Rubin properly objected to the admission of Cox's purported "prior consistent statements."

to decide that the rule should be consulted, I would in this case find that, "in fairness," the notes should not have been admitted. The government could have accomplished its purpose in this regard by means far less prejudicial. *Compare United States v. Lev,* 276 F.2d 605, 608 (2d Cir.), *cert. denied,* 363 U.S. 812 (1960), *with Camps v. New York City Transit Authority,* 261 F.2d 320, 322 (2d Cir. 1958). *See also United States v. Check, supra,* 582 F.2d at 682-83 n.43. Similarly, this appeal should not be decided by reference to some extension of the rule governing refreshment of present recollection.[9] I note as well that it is at least peculiar to treat the interview notes here in question as "statements" by Cox

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9 *See* note 1, *supra*. There can be no doubt, of course, that the notes were properly used to refresh Cox's present recollection of Rubin's statements during the interviews. *See Portman v. American Home Products Corp.,* 201 F.2d 847, 850 (2d Cir. 1953); *United States v. Rappy,* 157 F.2d 964, 967 (2d Cir. 1946), *cert. denied,* 329 U.S. 806 (1947); *Fanelli v. United States Gypsum Co.,* 141 F.2d 216, 217 (2d Cir. 1944). But this itself does not permit or call for the admission into evidence of the item used to refresh. The rule itself provides that only the "adverse party is entitled to have the writing produced at the hearing, to inspect it, to cross-examine the witness thereon, and to introduce in evidence those portions which relate to the testimony of the witness." Moreover, "the portions of the writing which the adverse party introduces may be supplementary in character rather than limited to credibility." 10 Moore's Federal Practice § 612.01 [1.-1], at VI-192. "It is fundamental that such memoranda are not admissible unless demanded by opposing counsel, in which event, of course, the purpose of the memoranda is to discredit rather than corroborate the witness's testimony." *Luse v. United States,* 49 F.2d 241, 243 (9th Cir. 1931). *See also Eisenberg v. United States,* 273 F.2d 127, 131-32 (5th Cir. 1959); *Portman v. American Home Products Corp., supra,* 201 F.2d at 850. *But see Markel Service, Inc. v. National Farm Lines,* 426 F.2d 1123, 1128 (10th Cir. 1970); *United States v. Rappy, supra,* 157 F.2d at 967-68.

of what Rubin had said at the interviews.[10] Nevertheless, assuming that the notes were properly deemed to be "statements" by Cox, *cf. United States v. Quinto, supra,* 582 F.2d 224; *Nager Electric Co. v. Charles Benjamin, Inc.,* 317 F.Supp. 645, 648 (E.D. Pa. 1970), *aff'd sub nom. Milwaukee Gear Co. v. Charles Benjamin, Inc.,* 466 F.2d 588, 591-92 (3d Cir. 1972), I turn to the question whether the notes were properly admitted, either for the purpose of bolstering Cox's credibility or as substantive evidence that Rubin had made certain statements during the course of the interviews.[11] In my judgment, it is quite plain that they were not properly admitted.

Judge Waterman has thoroughly explained the law regarding the admission of prior consistent statements in the recent decisions of *United States v. Check, supra,* and *United States v. Quinto, supra.* In *Quinto* he stated:

> For nearly 200 years last past, the courts have enforced, except in certain very limited cir-

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10 *Compare,* Fed. R. Evid. 801(a); Fed. R. Civ. P. 26(b)(3); 18 U.S.C. § 3500(e).

11 There can be no doubt that the government offered these notes at least in part as substantive evidence. At oral argument, Rubin's attorney asserted that the evidence had been offered both for the purpose of rehabilitating Cox's credibility and for the purpose of demonstrating the truth of the matters there asserted, the conditions for the latter being outlined in Fed. R. Evid. 801(d)(1)(B). The government attorney confirmed this view at the beginning of her argument:

> [T]he offer that the government made was not articulated as a Rule 801 offer but I think the rubric of the offer which is reprinted in the defendant's brief . . . makes it clear that although the government did not identify the rule by number it was offered as an 801 prior consistent statement.

That the notes were offered under Rule 801 is also assumed in the government's brief and borne out by the record.

cumstances, a general prohibition against the use of prior consistent statements. While it is true that the use of such statements to prove the truth of the matters asserted has always been clearly barred by the hearsay rule . . . the courts have also generally prohibited the use of such evidence even when the proponent of the prior consistent statement was simply offering it for the more limited purpose of bolstering the witness's damaged credibility. . . . The rationale for excluding most, but not all, prior consistent statements being offered to establish the witness's credibility is one of relevancy. 'The witness is not helped by [the prior consistent statement;] even if it is an improbable or untrustworthy story, it is not made more probable or more trustworthy by any number of repetitions of it." . . . There have been situations, however, in which courts traditionally have felt that it is indeed relevant to the issue of whether the witness's in-court testimony should be believed that on prior occasions the witness has uttered statements which are consistent with his in-court testimony. "Prior consistent statements traditionally have been admissible to rebut charges of recent fabrication or improper influence or motive." . . . But the prior consistent statements have been so admissible only when the statements were made prior to the time the supposed motive to falsify arose. . . . Only then was the prior consistent statement "relevant" on the issue of credibility; that is, it tended to make the trustworthiness of the witness's in-court testimony more probable, after that testimony had been assailed, inasmuch

> as the consistency of the prior statement with the witness's testimony at trial made it "appear that the statement in the form now uttered was independent of the [alleged] discrediting influence."

582 F.2d at 232-33 (footnotes and citations omitted).

The federal rules have not changed the law governing admission of prior consistent statements in order to "rehabilitate," the credibility of a witness. 582 F.2d at 233; Fed. R. Evid. 402. And while it is true that Rule 801(d)(1)(B)[12] changed prior evidentiary law to the extent that it declares that, under certain circumstances, prior consistent statements are not hearsay, and thus are not inadmissible under Rule 802, and thus are potentially admissible as substantive evidence, 582 F.2d at 233, the test for admissibility for either purpose continues to be the following:

> [T]o avoid having the prior consistent statement found irrelevant under Fed.R.Evid. 402 or incapable of satisfying the requirements of Fed.R.Evid. 801(d)(1)(B), the proponent must demonstrate three things. First, he must show that the prior consistent statement is "consistent with [the witness's in-court] testimony." . . . Second, the party offering the prior consistent statement must establish that the statement is

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12 The rule reads as follows:

> A statement is not hearsay if—[t]he declarant testifies at the trial or hearing and is subject to cross-examination concerning the statement, and the statement is . . . consistent with his testimony and is offered to rebut an express or implied charge against him of recent fabrication or improper influence or motive . . . .

> being "offered to rebut an express or implied charge against [the witness] of recent fabrication or improper influence or motive." . . . Finally, it is necessary that . . . the proponent must demonstrate that the prior consistent statement was made prior to the time that the supposed motive to falsify arose . . . .

582 F.2d at 233-34. *See also United States v. Check, supra,* 582 F.2d at 681 n.40 ("inasmuch as [the witness's] prior statements could not satisfy the standards set forth in Fed. R. Evid. 801(d)(1)(B), the statements were not admissible even for the more limited purpose of bolstering the witness's credibility"). Using this test,[13] error was committed.

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13 Despite the analysis in Judge Friendly's separate concurring opinion, it is my view that we are required to apply the same test whether the evidence is offered for purposes of rehabilitation or as substantive evidence. In *Quinto* the government offered the IRS memorandum into evidence "to rehabilitate one agent's damaged credibility and further to prove that Quinto had indeed made certain extremely incriminatory remarks to his inquisitors." 582 F.2d at 226. *See also* 582 F.2d at 229 ("the government attempted to introduce the memorandum as a prior consistent statement usable not only to corroborate [the agent's] in-court direct testimony but also usable under Fed. R. Evid. 801(d)(1)(B) as 'substantive evidence' to prove that Quinto had made the fatal admission the IRS agents claim he made"). The Court concluded: "[W]e *hold* that the memorandum should have been excluded regardless of whether it was offered for the truth of the matters asserted therein or merely for the more limited purpose of rehabilitating the in-court testimony of [the agent]." 582 F.2d at 232. I simply cannot bring myself to characterize this holding as mere "dictum." The fact that the parties in *Check* and *Quinto* did not choose to brief extensively the question whether the memorandum was admissible for purposes of rehabilitation as opposed to substantive evidence should not be used to detract from the strength of the express holding that it was not. *See Monell v. Department of Social Services of the City of New York,* 436 U.S. 658, 717-18 (1978) (Rehnquist, *J.*, dissenting) ("Private parties must be able to rely upon explicitly

To the extent that the notes labelled GX66A "say" that Rubin himself used the term "pay off" or the phrase "paid off" during the October 10 interview, they are consistent with Cox's testimony on direct. Arguably, therefore, the first prong of the three-part test for admission of prior consistent statements is met.[14] But I cannot say that the government successfully established that the notes were being "offered to rebut an express or implied charge against [the

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stated holdings of this Court without being obliged to peruse the briefs of the litigants to predict the likelihood that this Court might change its mind."). *See also id.* at 709 n.6 (Powell, *J.*, concurring) ("the mere fact that an issue was not argued or briefed does not undermine the precedential force of a considered holding").

Even were I to accept Judge Friendly's analysis on this matter, however, I would still feel constrained to characterize the notes as inadmissible. In my view, assuming dubitante that the notes are "relevant" to the issue of Cox's credibility, their "probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury . . . ." Fed. R. Evid. 403. In this regard, I note that even if the text of the notes had been offered as past recollection recorded under Fed. R. Evid. 803(5), the notes themselves could not have been admitted as an exhibit unless offered by Rubin. The reason for this limitation is quite apparently to prevent the jury from giving undue weight to the physical document itself. *See* McCormick, Law of Evidence § 299, 712-13 & n.8.

14 I say "[a]rguably" here because this points to the rather bizarre core of this portion of this appeal. Cox did not author the notes labelled GX66A; Levitt did. But Cox "adopted" them as statements by him of what Rubin had said at the interview. The notes imply that Rubin himself had used the phrase "paid off." On direct, Cox testified that Rubin had used that phrase during the interview. On cross, however, Cox testified that Rubin had *not* used it. Then on redirect the government offered, and the court received, GX66A as a "prior consistent statement" by Cox in order to support his testimony on direct that Rubin *had* said "paid off." As it turned out, of course, a subsequent government witness, Levitt, the author of GX66A, testified that Rubin had not used the incriminating phrase and that he (Levitt) had jotted it down as his own characterization of what Rubin had said.

witness] of recent fabrication or improper influence or motive," the second prong of the three-part test. During cross-examination, Bender began to ask Cox whether the agents had discussed with Rubin the issue of Rubin's being named as a defendant in any indictment resulting from the investigation. The government objected on grounds of relevance, and was granted a request to discuss the objection out of the hearing of the jury. At the side bar, Bender explained that he believed the agents had discussed immunity with Rubin but that they had conditioned it upon Rubin's presenting more precise information regarding the conduct of the other Tri-State principals. When Rubin failed to provide that information, Bender continued, the agents dropped the discussion of immunity and, apparently, recommended that Rubin be prosecuted. The government argued that such discussions could have no bearing whatsoever on Cox's truthfulness and should not be admitted as if they did. Bender responded that evidence of discussions of immunity "goes to Mr. Rubin's intent in meeting with these agents fully, in many instances without the lawyer, where he established a rapport with the agents and it certainly goes to show that he [Rubin] didn't believe he was guilty of anything and that is why he was talking." The trial court ruled against Bender, and the topic was not pursued. This is not sufficient evidence to support the government's claim that Bender had made "an express or implied charge against [Cox] of recent fabrication or improper influence or motive." The government successfully argued to the trial judge that the alleged discussions with Rubin about immunity could have no bearing on Cox's truthfulness; and Bender was

quite clear that the testimony he hoped to elicit from Cox would be used to demonstrate Rubin's motive while attending the interviews, not Cox's motive while testifying at trial. Although Bender did hint at such a motive during summation, by then the notes had long since been admitted. He should hardly be penalized for attempting to make the best of a bad situation. In addition, there was no determination by the trial court that the notes were admissible to rebut a charge of recent fabrication or improper influence or motive. *Cf. United States v. Herring,* 582 F.2d 535, 541 (10th Cir. 1978); *United States v. Zito,* 467 F.2d 1401, 1404 (2d Cir. 1972). Finally, the government did not demonstrate, in any fashion whatsoever, that the notes were made "prior to the time that the supposed motive to falsify arose," the third prong of the three-part test. Given the general disfavor with which prior consistent statements have been, and are to be, treated in the federal courts, the proponent of such evidence has a heavy burden in justifying admission. That burden was not met here.

Thus there was error. I do not believe that it was harmless error. Again making reference to Judge Waterman's *Quinto* opinion, the standard for determining whether an error of the type committed during the trial below is harmless is as follows:

> Regardless of whether there were other independently sufficient evidence to convict the defendant, we can find the error harmless only if "our conviction is sure that the error did not influence the jury or had but very slight effect...."

582 F.2d at 235, *quoting United States v. Ruffin,* 575 F.2d 346, 359 (2d Cir. 1978), *quoting Kotteakos*

v. United States, 328 U.S. 750, 764 (1946). I have no such sure conviction here, especially with regard to the admission of GX66A. Rubin at no time denied having made payments of cash to Ludwig and Keating, but he at all times denied making "payoffs" or "bribes." Indeed, these payments were the "central core" of the government's case against Rubin, so described by the government during trial. Bender had succeeded at calling into question Cox's assertion that Rubin had said during the January 9 interview that he (Rubin) had said to Ludwig, "Look, Ray, if you can see your way clear to help us, we will take care of you." This, of course, went directly to the issue of Rubin's knowledge and intent regarding the payments. Bender had also succeeded at getting Cox to acknowledge on cross that Rubin himself may not have used the terms "pay off" or "bribe." For the government to then introduce the notes as prior consistent statements by Cox, purportedly tending to show either that Cox was being more credible on direct than on cross regarding Rubin's precise statements or that Rubin had in fact used those terms could have been nothing less than damaging to Rubin's defense. The fact that the jury asked for the notes during its deliberations and the fact that the jury acquitted Rubin on the substantive count but convicted him on the conspiracy count serve only to buttress my conviction that, far from being harmless, the introduction of these notes into evidence was harmful.

For these reasons I would reverse the judgment of conviction and order a new trial; for these reasons I dissent.

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

DOCKET NO. 78-00075-03 CBM

UNITED STATES OF AMERICA

vs.

WILLIAM RUBIN

Defendant

In the presence of the attorney for the government the defendant appeared in person on this date June 30, 1978

Counsel

[x] With counsel Louis Bender

Plea

There being a verdict of [x] Guilty.

Finding & Judgment

Defendant has been convicted as charged of the offenses of conspiring to commit the following offenses; to wit, 15 U.S.C. §77q(a), and 18 U.S.C. §§ 1341, 1343 and 1014 as charged in Count One (1) of the indictment in violation of Title 18, United States Code, Section 371.

Appendix B

Sentence or Probation Order

The defendant is hereby committed to the custody of the Attorney General or his authorized representative for imprisonment for a period of Three (3) Years.

Count Two (2) of the indictment is dismissed upon the motion made by the Government at trial.

The defendant is Acquitted of Count Three (3) of the indictment by the verdict of the jury of Not Guilty.

Special Conditions of Probation

Defendant's application for a stay of this judgment pending appeal is Denied on the ground that it appears that the proposed appeal is frivolous, no ground for appeal having been assigned, and it is taken wholly for the purpose of delay. This is supported further by the fact that no exceptions to the charge were made and no post-trial motions were filed by the defendant.

Additional Conditions of Probation

In addition to the special conditions of probation imposed above, it is hereby ordered that the general conditions of probation set out on the reverse side of this judgment be imposed. The Court may change the conditions of probation, reduce or extend the period of probation, and at any time during the probation period or within a maximum probation period of five years permitted by law, may issue a warrant and revoke probation for a violation occurring during the probation period.

Commitment Recommendation

The Court orders commitment to the custody of the Attorney General and recommends,

Appendix B

It is ordered that the Clerk deliver a certified copy of this judgment and commitment to the U. S. Marshal or other qualified officer.

Signed by

[x] U.S. District Judge CONSTANCE BAKER MOTLEY

Date June 30, 1978

U.S. District Court
S. D. of N.Y.
Filed Jun 30 1978

JOINT APPENDIX

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

No. 79-1013

WILLIAM RUBIN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITION FOR CERTIORARI FILED DECEMBER 19, 1979

CERTIORARI GRANTED APRIL 14, 1980

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JOINT APPENDIX

Relevant Docket Entries

Date	*Proceedings*
1-27-78	Filed Indictment and related to 78-cr-76. . . . Motley, J.
2- 2-78	Defendant (attorney present) pleads not guilty.
3-22-78	Filed affidavit of Louis Bender in support of motions addressed to the indictment.
4-10-78—	Filed Affidavit of R. K. Neugarten, AUSA, in opposition to defendant's omnibus motions.
4-10-78	Filed Government's memorandum in response to omnibus motions.
5- 8-78	Defendant and attorney present. Jury trial commenced.
5- 9-78-5-25-78	Trial continued.
5-26-78	Trial continued and concluded. Jury finds defendant Guilty on Count 1; Count 2 is DISMISSED on Government's motion; Not Guilty on Count 3. Sentence 6-30-78. Bail continued. Motley, J.
6-30-78	District Court Judgment set out in Appendix B to the Petition for Certiorari.
6-30-78	Filed NOTICE OF APPEAL of Defendant to United States Court of Appeals for the Second Circuit from Judgment of conviction.
7-6-78	Filed True Copy of United States Court of Appeals Order that motion is granted to the extent that surrender is stayed until July 5, 1978 by which time the court can consider the motion on a complete record.

Relevant Docket Entries

Date	*Proceedings*
7-11-78	Filed True Copy of United States Court of Appeals Order granting continuation of appellant on bail and under same conditions Re: determination of appeal and that a briefing schedule be arranged promptly.
6-30-78	Filed Transcripts of Record of Proceedings dated: May 8, 9, 10, 11, 12, 15, 16, 17, 18, 19, 22, 23, 24, 25, 26, 30, 1978.
	Judgment of the District Court affirmed in an Opinion dated September 6, 1979, set forth in Appendix A to the Petition for Certiorari.
	The issuance of the mandate stayed by the Court of Appeals on October 10, 1979 pending application to this Court for a writ of certiorari.
	Petition for rehearing and in the alternative for a hearing en banc denied by the Court of Appeals on November 20, 1979.

Relevant Portions of Trial Transcript

* * *

[210]* JOHN JOSEPH KEATING, called as a witness on behalf of the government, having first been duly sworn, testified as follows:

(Direct Examination)

* * *

[216] Q. What were the general nature of the kinds of corporate loans that were done out of that branch in 1972 as you knew it? [217] A. By industries?

Q. By industries? A. About half of the loan portfolio was to garment center, mostly women's wear manufacturers and the other 50 percent was spread amongst several industries really with no concentration at all.

Q. Was a written loan application customarily used for corporate loans of Bankers Trust? A. No, there was no written loan application.

Q. How would a corporation obtain a loan? A. Basically they would come into the bank, they would present financial statements on the corporation, they would give a general resume of what the corporation did and what business they were involved with, a description of their—of the officers of the corporation and generally, in most instances, the bank would ask for a projection. If they were asking for a loan, a projection was merely a form of indicating how they were going to pay the loan back.

Q. A projection of what? A. Basically of cash flow, generally, mainly whatever sales were going to be gen-

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* Figures in brackets refer to the page of the Stenographic Transcript.

erated over whatever period of time and how these sales would be turned into cash over another period of time to pay the loan off.

Q. Did bank procedures let a loan office make a loan [218] by himself or herself? A. No, Bankers Trust required two signatures on—for a loan to be approved, and both signatures—the officers who signed the loan application both had to have authority equal to cover the amount of the loan.

Q. When you say authority equal to the limit, what kind of authority are you talking about? A. Lending authority. The bank assigns to each lending officer a certain amount of lending authority, meaning maybe you would have 100,000 or 200,000 dollars in authority. In other words, the bank was giving you the right to make that amount of loan with another lending officer.

Q. So, you could loan—if you had $100 thousand authority, you could make a loan up to $100 thousand? A. That's right.

[219] Q. Do you recall what lending limit you personally had in 1972, the latter half of 1972? A. I am not exactly certain. I think it was a hundred or $200,000. It was one or the other. I know it was increased during that period. I am not exactly sure when it was increased.

Q. When a loan was made by a branch, in your case, the Seventh Avenue branch, under what circumstances if any would it be reviewed by somebody outside of your branch? A. Generally you could send a copy of a memo covering the transaction to an area of the bank called "loan administration", but the branch really had the authority to make loans without sending—without any concurrence from anybody else up to a half million dollars.

Q. Above a half million dollars, that is $500,000, was there a different procedure? A. Above a half million

dollars there were two people at the branch that had what was described as the unlimited lending authority of the bank; in other words, they could lend up to the legal limit.

Every bank has a limit imposed on it by the Federal Reserve System where you are not allowed to lend more than 10 per cent of your capital and surplus.

[220] At that time, Bankers Trust had, I believe, somewhere around $67 million in legal lending limit. Ray Ludwig had legal lending limit authority or unlimited authority, so if a loan was going out of the office, he would have to get the concurrence of somebody else in Loan Administration for anything above $500,000.

Q. So in other words, if Mr. Ludwig wanted to make a loan of $525,000, he needed somebody outside of your branch? A. Exactly.

Q. But anything—$500,000 or less, he was the highest authority? A. That's correct.

• • •

[221] Q. Did there come a time in 1972 when you heard of a [222] company called Tri-State Energy? A. Yes. I first heard of Tri-State Energy on October 19, 1972.

Q. Do you recall the circumstances under which you heard of Tri-State Energy? A. Yes. There was—was late in the afternoon. It was after banking hours had closed. There was a meeting going on at Ray Ludwig's desk which was in clear sight of my desk. The way the lending officer seats were arranged was on a long narrow corridor, almost like the jury box over here. There was a meeting going on, there were three gentlemen there

with Mr. Ludwig, and Mr. Ludwig—I could see conversations going on—called me over, informed me that we were going to be making a loan to Tri-State Energy which he said was a coal company, that the loan would be booked tomorrow because it was after banking hours at that particular time, and that I should go back to my desk and open up checking accounts and get the normal information that you would when you would be starting a new relationship from a company.

Q. When you say it was after banking hours, what was the close of banking hours at that time? A. Three o'clock, so it was somewhere between—after three. I am not exactly sure.

[223] Q. Did Mr. Ludwig introduce you to the three persons with whom he was? A. Yes, he did.

Q. Do you recall their names? A. C.W. Deaton, William Rubin and Leonard James.

Q. Do you recognize anyone in the courtroom today? A. Yes, I do.

Mr. Bender: That identification is conceded.

Ms. Neugarten: The identification of the defendant Rubin, I assume.

Mr. Bender: None other.

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[225] Q. Were you told what the loan was for? A. I believe that the initial loan was for payroll at the mine.

• • •

Q. Did you do any paper work with respect to that loan on that date? A. Yes, we took in several documents, including the note itself which is like the equivalent of

an IOU from the corporation, and we had deposit resolutions, borrowing resolutions and corporate guarantees of the three principals.

* * *

[228] specific conversations that you mention, what positions the three people have at Tri-State? A. Leonard James was the president of the corporation, C.W. Deaton was secretary-treasurer, and William Rubin was the vice-president.

Q. Was the loan to be effective that day, October 19 or some other time? A. No, it couldn't be effective that day because the loan had to be processed by the clerical staff. They were—it was past banking hours, so that couldn't be done. The loan was to be effective the next day, on the 20th of October.

Q. That's 1972? A. Yes, sir, 1972.

Q. How was Tri-State to obtain the money that was borrowed? A. The money was to be credited to their checking accounts.

Q. At what bank? A. Bankers Trust, Seventh Avenue Branch.

Q. That was the checking account that you opened on that day? A. Yes, that's correct.

Q. Were they to get $50,000 or some other amount? [229] A. It was a liability less than $50,000. The way Bankers Trust processed loans, they discounted the interest in advance. What they did was they deducted whatever one month's interest was from the proceeds of the loan so they would receive $49,000 and some hundreds.

I would have to see the note to know the exact amount, but it was something less than $50,000.

John Joseph Keating—for Government—Direct

Q. Did there come a time that Bankers Trust received initial collateral on that loan? A. Yes.

Q. Do you recall when that was? A. I believe it was delivered to the bank on the 20th of October. It was a stock certificate, and I knew that the stock certificate was coming in because on the 19th, during the conversations, Ray Ludwig told me that we would be receiving collateral on the loan.

Q. Do you recall who brought in the stock certificate? A. It was Rubin or Deaton or both, perhaps, I am not certain at this time.

• • •

[233] A. Government's Exhibit 6 is a stock certificate for a company named American Leisure Corporation. The stock certificate is registered in the name of Tri-State Energy. It is for 400,000 shares and there is a legend on the stock meaning that the stock is restricted.

Q. Now, is this the stock certificate which you earlier testfied you received as collateral the next day which is October 20, 1972? A. That's right.

Q. Now, Government's Exhibit 7 and Government's Exhibit 8 for identification, two separate pieces of paper. A. Okay.

Government's Exhibits 7 and 8 are stock powers signed by Tri-State Energy and by C. W. Deaton with the signature guaranteed by Chelsea National Bank, an officer of that bank guaranteed that this was the signature of C. W. Deaton.

And the stock powers would be used by a bank [234] when they would be accepting marketable securities as collateral so that they could sell them if they had to at some future date.

Q. Now, both Exhibits 7 and 8 are stock powers, is that correct? A. Yes.

Q. Now, do you have a precise recollection of when you received those stock powers? A. I imagine it would have been the day that the stock was delivered, because that would be standard policy. I can't recall specifically, but if you were receiving a stock and you didn't have the stock powers you really wouldn't have collateral.

Q. But they are not dated, is that correct? A. No, they are not.

• • •

[235] Q. Now, Government's Exhibit 9 for identification, can you identify this document? A. Yes, I can.

Government's Exhibit 9 is what Bankers Trust Company calls an offering ticket. And what this is basically is the vehicle whereby a loan is put on. Okay? This creates the loan in the bank. And the information on the offering ticket gives the date of the loan, the name of the company, the amount, the maturity date, the rate of interest being charged, whether the loan is a new loan or a renewal of an already existing loan, what type of loan it is, if there are any guarantees involved and who the guarantors are.

And if we have any collateral for the loan. And also, it gives the initials of the two lending officers who create the loan.

• • •

[237] A. Right.

Q. Do you see the words "Tri-State Energy"— A. Right.

Q. —printed on the front of them? A. Right.

Q. I mean hand printed on the front of them. Do you recognize the handwriting? A. Ray Ludwig's printing.

John Joseph Keating—for Government—Direct

Q. And the offering ticket, Government's Exhibit 9 in evidence, by whom is the information on this offering ticket filled out? A. The information on the offering ticket is filled out by clerks, they called it the general cage in the bank, that was the jargon for the area who prepared this—

* * *

A. It was prepared by clerks. The general case was [238] the name of the area who prepared the offering ticket.

Q. Now, you see a column "R or N"? A. Yes.

Q. What does that mean? A. That means whether the loan is a new loan or whether it is a renewal of an existing loan.

Q. And what is the indication on that offering sheet, Exhibit 9 in evidence? A. It's a new loan.

Q. Now you see a column labeled "Rate"? A. The rate on the loan was 7 percent.

Q. That refers to the interest? A. Yes.

Q. And you see a note "RA"? A. Yes. There is a—printed there it says "Lien Stock, 400,000 shares American Leisure Corp."

Q. And to what does that refer? A. To the stock that was given as the collateral for the loan.

Q. So in other words, the collateral is lien stock? A. No, the lien stock is when a bank—basic jargon that was used in the bank at that time was that when you were taking collateral, side collateral for a loan, you would say lien stock of whatever numbers of shares it would [239] be.

Q. Now, when you said "side collateral," can you tell us what you mean by that? A. Well, when the loan was made initially, the loan was envisioned that it would be

repaid from the ongoing operations of the corporation, namely from the sale of coal or natural gas. The collateral was taken as a secondary source of repayment in the event that the primary source, the ongoing operations of the corporation didn't materialize.

* * *

[241] Q. Now, directing your attention from Government's Exhibit 1, next to Government's Exhibit 6 in evidence, you see a red stamp. A. Yes.

Q. Could you read it out loud as best you can? It is printed over other writing, I believe. A. "The shares by this certificate is unregistered [242] stock, and these shares may not be sold, disposed of or otherwise distributed without, one, complying with the registration requirements of the Securities Act of 1933 as amended, and these rules and regulations thereunder, or, two, without obtaining an opinion of American Leisure Corp.'s counsel that the proposed disposition of said shares is"—and I can't make out the last line.

Q. Now, before you got this particular collateral on October 20th, had you ever seen a stamp of a similar kind on a stock certificate before? A. Yes.

Q. And have you since? A. Yes, I have.

Q. And what did you understand it to mean? A. Well, basically, it is a restriction having to do with some insider information on a stock. Basically, the stock—it is not marketable in a broad sense. It can be sold, but the only amount of the stock that can be sold is predicated on I think the activity for the prior six months or year, a certain percent of that activity.

Q. Now, as a practical matter, did that have any significance—does that have any significance to the worth of a

stock certificate as collateral? A. Because it isn't as marketable as an unrestricted [243] stock, the worth of the collateral is substantially reduced, because if you had to sell the stock, you could only do it in dribs and drabs over a long period of time. You couldn't sell it all at once.

Q. So this certificate would have been more valuable if it didn't have that stamp? A. Yes.

Q. To you, for collateral. A. Yes.

Q. Now, do you see—would you read the line beginning "This certifies"? A. "This certifies that Tri-State Energy, Inc. is the owner of"—keep on going?

Q. Yes. A. —"400,000 fully paid and non-assessable shares of common stock without par value of American Leisure Corporation"—

Q. Okay, stopping there.

What did you understand that to say? A. That Tri-State was the owner of the stock.

Q. Now, were you at any time ever told by Rubin, Deaton or James, anything to the contrary? A. No.

Mr. Bender: I object to that. I object to the [244] form of the question, your Honor.

The Court: Well, I gather the suggestion is it is leading?

Mr. Bender: Also, I think the question ought to be directed to whether Mr. Rubin ever said anything, not what somebody else said. This man has indicated that he's been at the bank, he has met Mr. Rubin and in I don't know what period of time we are referring to in this question.

Q. The question is at any time. An open-ended question.

The Court: At any time.

A. At no time did they say that this was anything else but their stock.

Q. Now, at the time you received this, which was October 20, 1972, what did you understand to be the relationship between restrictions on stock and stamps like this red stamp on stock certificates? A. At that time I believed the only way a stock could be restricted was if it had this stamp on the certificate.

Q. Have you generally discovered whether you were correct or incorrect in your belief? A. I was incorrect.

Q. And you have learned that stock can be [245] restricted and not have a stamp? A. Yes. It can be restricted through—by means of a letter called an investment letter that's attached to the stock certificate with no stamp on the face of the certificate itself.

Q. Now, did Bankers Trust have any policy regarding whether or not restricted stock could be received as collateral? A. No, there was no policy.

The way a banker would look—a banker generally looks at any loan and says that collateral makes any loan better. So to that extent that we had restricted stock, it was better than if we had nothing at all. However, obviously the preference of any lending officer was to have unrestricted stock so that if anything went wrong with the loan he would be in a position to sell it right away instead of over an extended period of time.

Q. Now, again, do you recall who brought you that stock certificate, Government's Exhibit 6? A. It was Rubin or Deaton or both.

Q. And that was on October 20th? A. Yes.

Q. And did you have any conversation with the person or persons who brought you that certicate? [246] A. Yes, I had a conversation with him and specifically what was said it was that it was fine that they were bringing in the

restricted stock, but the desire of the bank was to get good marketable collateral and we were informed by either Deaton or Rubin, or perhaps both of them, that we would be getting good marketable collateral in the future and we would be getting New York Stock Exchange collateral.

Q. Were you told anything regarding the restriction on this particular stock? A. Yes. It was indicated—I can't recall who said it—but that the restriction would be released at some future date.

Q. When you say you can't recall who said it, who were the— A. Well, it would have been either Deaton or Rubin or both of them perhaps.

Q. But one of those two at least? A. One of those two.

Q. Now, did Tri-State in fact ever bring you unrestricted American Leisure stock? A. No.

Q. And did they ever in any way remove the stamp from the American Leisure stock? [247] A. No, they did not.

Q. Now, when you got the stock, the American Leisure did the person or persons who brought it to you tell you how it had been obtained by Tri-State? A. Yes. The conversation that I recall having with Deaton or Rubin or both of them was that they had gotten the stock in a coal swap. In other words, they had a mine in Kentucky and they traded part of the rights to, a certain amount of coal in that mine, in exchange for the stock.

Q. Now, as of October 20, 1972, or after October 20, 1972, and during the next month, that would be up to and including November 20, 1972, did you ever talk to Rubin or Deaton? A. I talked to both of them on just about a daily basis, both in person and on the phone.

Q. And was that both of them together or separately? A. In both manners, they came in together on several occasions and they came in separately on several occasions.

Q. And do you recall of the two of them, that is Rubin and Deaton, whom you saw and talked to the most? A. Rubin.

Q. Now, did there come a time that Bankers Trust made another loan to Tri-State? [248] A. Yes.

Q. Now, handing you Goverment's Exhibits 11, 12 and 13 for identification, and referring to them again by number, would you identify each of those documents for the Judge and jury? A. Government's Exhibit 11 is another note that was dated November 20, 1972 for $50,000, and it was signed by C. W. Deaton of Tri-State Energy, Inc.

Q. Now, do you recognize his signature on that? A. Yes, I do.

Q. And turning to Government's Exhibit 12 for identification? A. Government's Exhibit 12 is a note for $50,000 dated November 22, 1972 by Tri-State Energy, Inc., signed by C. W. Deaton.

Q. And do you recognize his signature? A. Yes, I do.

Q. And does this note bear any initials on it? A. Yes, it bears the November 22nd note which is Government's Exhibit 12, it bears my initials and the note dated November 20th, which is Government's Exhibit 11 bears Ray Ludwig's initials.

Q. Now, when you say initials as to Ludwig—

Ms. Neugarten: Strike that.

[249] Q. Government's Exhibit 13 for identification. A. Government's Exhibit 13 is an offering ticket, it means the way a loan is created, dated November 22, 1972. It is for Tri-State Energy, Inc. and it reflects two loans being paid, one for $50,000 with a maturity date of February 22nd, and one for $50,000 with a maturity date of February 20th.

The February 22nd maturity date is a new loan and the February 20th maturity date is a renewal of the loan that was placed on October 20th and had matured.

The loans are guaranteed by Deaton, James and Rubin, and we continue to hold in lien stock the 400,000 shares of American Leisure Corporation.

Q. Now, is that initialed by anyone? A. Yes, it is initialed by Ray Ludwig and me.

Q. And the two loans to which Government's Exhibit 13 for identification pertains are the loans which are documented by Government's Exhibits 11 and 12 for identification? A. Yes. That's true.

> Ms. Neugarten: Your Honor, at this time the government offers Government's Exhibits 11, 12 and 13 for identification into evidence as Government's Exhibits 11, 12 and 13.
>
> Mr. Bender (handing).
>
> [250] Mr. Bender: I have no objection, your Honor.
>
> The Court: All right. Government's Exhibits 11, 12 and 13 are received.
>
> The Clerk: Government's Exhibits 11, 12 and 13 are received in evidence.
>
> (Government's Exhibits 11, 12 and 13 were received in evidence.)

Q. Now, directing your attention to Government's Exhibit 13 in evidence, you noted that it refers to guarantees of three people, is that correct? A. Yes.

Q. Now, did you obtain a second or new guarantee form at that time? A. No.

Q. And was there a reason why you did not? A. It wasn't necessary. The initial guarantee covers all and future loans that would be granted.

John Joseph Keating—for Government—Direct

Q. And what do you understand to be an unlimited guarantee which I believe is how you characterized those three guarantees that we have seen? A. The people who execute the guarantee, in this case Rubin, Deaton and James, guaranteed the loan regardless of how much it would be. If we had made a $100 million loan to the company they would be guaranteeing the full $100 * * *

* * *

[253] Q. Now, when the clerical staff went to fill in in cases where they did a value for collateral, do you know how they would do that? A. They would either get it from the newspapers or from documents that were called pink sheets because of this color which had the prices of stock that wasn't traded on either the New York or American Stock Exchange, what is called over-the-counter securities.

Q. So do I understand that for stock exchange traded stock they would go to the newspaper and for over-the-counter stock that was listed in the pink sheets, they would [254] go to this thing called the pink sheets? A. That's correct.

Q. Now, at the time that you got the loans—or you made the loans embodied by Government's Exhibits 11 and 12, did you have any conversations with anyone from Tri-State? A. Yes, I did. I spoke to Rubin or Deaton or both, and this particular—the loan itself was again for payroll, and again we were talking about getting additional marketable collateral which would be New York Stock Exchange collateral.

* * *

[255] Q. Now, directing your attention to Government's Exhibits 14 and 15 for identification, can you identify them for us (handing)? A. Yes.

Government's Exhibit 14 is a $100 thousand loan which is dated November 30, 1972, and it is signed by Tri-State energy. It was for three months. And again, they didn't [256] receive the full amount of the loan. In this instance the actual dollars received were $98,250 in one set and the interest that was discounted was $1,749.99.

Q. And you said it's signed by Tri-State. By whom? A. C. W. Deaton

Q. And Government's Exhibit 15 for identification? A. Government's Exhibit 15 is an offering ticket representing the granting of this loan, $100 thousand.

Again, the guarantees continued to be enforced of Deaton, James and Rubin, and we continued to hold the 400,000 shares of American Leisure as collateral.

• • •

[258] Q. Now, handing you what has been marked as Government's Exhibit 21 for identification, do you recognize that document (handing)? A. Yes, I do.

This is a demand note rather than a time note which the others were, meaning that these loans ran for a specific period of time.

This loan, this document here, Exhibit 21, was a loan that was payable on demand of the bank.

Q. And by whom is it signed? A. It is signed by Leonard James.

Q. Was that signature affixed in your presence? A. It was signed in my presence.

Q. And that is as distinguished from the other notes that you have referred to? A. Yes.

Q. And does it bear your initials on it? A. Yes, it does.

Ms. Neugarten: Your Honor, at this time the government offers Government's Exhibit 21 for identification in evidence as Government's Exhibit 21.

Mr. Bender: No objection.

The Court: Received. Government's Exhibit 21 is received.

[259] Q. Now, returning to Exhibits 14 and 15, again the offering sheet, Government's Exhibit 15 in evidence, was that prepared in the same way as the other offering sheets that you have discussed? A. Yes, it was.

Q. And it that described as a renewal or a new note? A. New loan.

Q. And this was for an additional $100 thousand beyond that that you previously loaned? A. It was a $100 thousand in new money.

Q. And at that point the total indebtedness of Tri-State to Bankers Trust was how much? A. $200 thousand.

Q. And did you have a conversation with anyone regarding this loan? A. Yes, I did.

Q. And do you recall with whom you had that conversation? A. Rubin or Deaton or both of them. And the basic conversation went along the lines that this loan would be used for small equipment purchases, as well as payroll.

[260] Q. And that's for the mining operation? A. Yes.

Q. Now, did there come a time that Tri-State borrowed further money? A. Yes.

John Joseph Keating—for Government—Direct

Q. And handing you Government's Exhibits 16 and 17 for identification, can you—do you recognize those documents? A. Document—or Government's Exhibit 16 is a note for $275 thousand dated December 6, 1972, signed by C. W. Deaton on behalf of Tri-State Energy.

Q. And does it bear your initials? A. Yes, it does.

Q. And do you recall whether or not Mr. Deaton signed it in front of you? A. No, I do not. It is possible that this could have been signed in blank.

Q. Now, directing your attention to Government's Exhibit 17 for identification. A. Government's Exhibit 17 is an offering ticket dated December 6, 1972. It shows $275 thousand with a maturity date of 3/6. It is a new loan, at 7 percent, and the loans continued to be guaranteed by Deaton, James and Rubin.

[261] We now have lien stock of $750 thousand, and it is signed by me, Ray Ludwig, and it has the initials of another lending officer named Jerry Weiner.

• • •

Ms. Neugarten: At this time the government offers Government's Exhibits 16 and 17 for identification into evidence as Government's Exhibits 16 and 17.

(Documents handed to Mr. Bender.)

Mr. Bender: No objection, your Honor.

The Court: Received. Government's Exhibits 16 and 17.

(Government's Exhibits 16 and 17 were received in evidence.)

• • •

[279] Q. As of December 6, 1972, once this note, Government's Exhibit 16 for $275,000 was signed, what was [280] the total amount of the indebtedness of Tri-State Energy to the bank at that time? A. $475,000.

Q. Were you ever told by anyone at Tri-State the purpose for the $275,000 loan? A. Yes. Rubin told me the $275,000 loan was to buy a mining machine called an auger.

Q. Do you recall when you had that conversation with Mr. Rubin? A. Some time in the beginning of December. It could have been on the 6th, I am not certain.

Q. In the month commencing December 6, 1972, and running until January 6, 1973, did you have any other occasion or did you have any occasion to speak to Mr. Rubin? A. Yes, several times, both in person and on the telephone.

Q. Did you speak to Mr. Deaton at all during that period? A. Yes. There were several occasions where I spoke to Mr. Deaton also. At that time the primary contact person was Mr. Rubin.

Q. By "that time," you mean what time? A. December to January of 1972 and early 1973.

Q. Handing you what have been marked as Government [281] Exhibits 18, 19 and 20 for identification, would you tell us what those documents are by number, please? A. Government Exhibit 18 is an unlimited guarantee signed by C.W. Deaton. It isn't dated on the back. On the front there is a stamp dated November 17, 1972, and it is guaranteeing the debt of Tri-State Energy.

Q. Do you recognize the signatures of Mr. Deaton on that document? A. Yes, I do.

Q. Addressing yourself to Government Exhibit 19 for Identification. A. Government Exhibit 19 is a Bankers

Trust form called a power of attorney to endorse securities. It is signed by C.W. Deaton and dated the 27th day of November, 1972.

Q. The handwriting filling in that date, whose is that? A. The date is my handwriting.

Q. Do you recognize the signature of Mr. Deaton? A. Yes, I do, that's Mr. Deaton's signature.

Q. Addressing yourself to Government Exhibit 20 for identification. A. Government Exhibit 20 is a corporate resolution to transfer of securities. This is another Bankers Trust [282] form, and it is signed by Deaton and the signature is guaranteed by me.

Q. Is that your signature where the guarantee is? A. Yes, it is.

Q. Do you recognize the signature of Mr. Deaton? A. Yes, I do.

> Ms. Neugarten: Your Honor, at this time the Government offers Government Exhibits 18, 19 and 20 for identification into evidence as Government Exhibits 18, 19 and 20.
>
> Mr. Bender: No objection.
>
> (Government Exhibits 18, 19 and 20 were received in evidence.)

• • •

[283] A. When you take stock as collateral, there are two ways in which you have the right to sell it; Number 1, you can take stock powers as we did when the American Leisure stock was delivered to the bank.

The second way you can do it is to get a blanket form called a power of attorney to endorse securities. This

form can be used in lieu of stock powers to cover various amounts of securities; in other words, if you have got tons of certificates, this one form would be used in lieu of getting an equal amount of stock powers.

It was just an effort to save paper.

The second document, corporate resolution on the transfer of securities is just a document that authorizes the bank, in other words, the corporation, meaning Tri-State Energy, is authorizing the bank that they are giving it the right to sell, assign, transfer or dispose of any stocks, bonds or other securities which the bank may hold as collateral.

Q. Before getting to the next note, was there a reason why you obtained that power of attorney and those corporate resolutions? [284] A. Yes, because we were in the process of receiving additional collateral for the loan and in addition to that we were promised on many occasions that we would be receiving New York Stock Exchange collateral in the future.

Q. Handing you Government Exhibit 21 already in evidence and Government Exhibit 22 and 23 for identification, would you first indicate if you recognize Government Exhibits 22 and 23 for identification and indicate what they are? A. Yes, Government Exhibit 22 is an offering ticket which creates a loan. This is dated February 26, [1973], with Tri-State Energy, Inc. being the borrower. It is for $475,000, payable on demand. It is recorded as a new loan and the rate of interest is 12 per cent. It continues to have the guarantees of Deaton, James and Rubin, and there is writing on it meaning that there is lien collateral of stocks and bonds and it is signed—not signed, but it is initialed by me, Ray Ludwig and it has Jerry Weiner's initials also.

• • •

[289] Q. Did you ever receive any collateral from Tri-State other than the American Leisure Corporation stock? A. Yes, I did.

Q. Directing your attention—

Mr. Bender: Excuse me. Was that question him personally or the bank?

Ms. Neugarten: The bank.

A. The bank received it.

Q. Directing your attention to Government Exhibits 24, 25, 26, 27, 28, 29 and 30 for identification, do you recognize them? A. Yes, I do.

Q. Would you identify them by number, please? A. Government Exhibit 24 is a stock receipt [290] form issued by the Bankers Trust Company indicating that we had received as collateral 1000 shares of Allstate Life Insurance registered in the name of Tri-State Energy and 1000 shares of Allstate Life Insurance Company registered in the name of Owen J. Oons.

Q. That is a business record of Bankers Trust Company? A. Yes, it is.

Q. And Government Exhibit 25 for identification? A. Government Exhibit 25 is a stock certificate for 1000 shares of Allstate Life Insurance Company registered in the name of Tri-State Energy.

Q. To the best of your recollection, is this the stock certificate, this Government Exhibit 25, that Bankers Trust actually received? A. To the best of my knowledge, it is.

Q. And Government Exhibits 26 and 27 for identification, what are they? A. Government Exhibit 26 and Government Exhibit 27 are stock certificates for Allstate Life Insurance Company, each of them representing 500 shares of stock, and they are both registered in the name of Owen J. Oons.

Q. To the best of your knowledge, are these the certificates actually received by Bankers Trust Company? [291] A. Yes.

Q. And Government Exhibits 28 and 29 for identification? A. Government Exhibits 28 and 29 are stock powers both signed by Owen J. Oons and guaranteed by both the North American Planning Corporation and by the Chelsea National Bank.

Q. Are those signatures with which you had personal familiarity? A. No, they were not.

Q. From whom or from what company did Bankers Trust recieve these stock powers? A. They received the stock powers from Tri-State Energy.

Q. Directing your attention to Government Exhibit 20 for identification, or 30 for identification, rather. A. Government Exhibit 30 is a corporate resolution of Tri-State Energy, Inc., signed by C.W. Deaton and Leonard James and the signature is guaranteed by the Chelsea National Bank, and the resolution authorized Leonard James and/or C.W. Deaton to sign any and all papers necessary or caused to be arranged alone on Allstate Life Insurance Company stock.

[292] Q. And this is a photocopy, is that correct? A. Yes, it is.

Q. Does the signature of Mr. Deaton appear to you to be the signature of Mr. Deaton? A. Yes, it does.

Ms. Neugarten: At this time the Government offers Government Exhibits 24 through 30 for identification into evidence as Government Exhibits 24 through 30.

Mr. Bender: I have no objection, your Honor.

The Court: All right.

(Government Exhibits 24 through 30 were received in evidence.)

Q. Directing your attention to the stock certificates, Government Exhibits 25, 26 and 27 in evidence, were these received by the bank as collateral? A. Yes, they were.

Q. And do they bear any stamp of the kind that was on the American Leisure stock certificate? A. No, they do not.

Q. Do you recall at what point Bankers Trust received these three certificates as collateral? A. If I can use this as a reference.

Q. To what are you referring? A. Exhibit 24.

[293] The bank received the stock certificates as collateral on or about November 10, 1972.

Q. At what point in time would this Government Exhibit 24 in evidence be prepared? A. In theory it should be prepared on the day that the collateral is received.

Q. Was that in fact always precisely the case? A. Not always, but I would say most of the time.

Q. If there was a variation, by about how much was there a variation? A. One or two days, that is about it.

Q. Handing you Government Exhibit 31 for identification, do you recognize this document? A. Yes, I do.

Q. What is it? A. Government Exhibit 31 is a stock receipt form issued by the bank, dated December 6, 1972, representing that we received 100,000 shares of Management Dynamics, Inc. stock, and it was collateral for Tri-State Energy loan.

Q. Do you recall whether at some point Management Dynamics, Inc., stock was received as collateral? A. Yes, I do.

Q. Was it received? A. Yes, it was. It would have been on or about [294] December 6, 1972.

Ms. Neugarten: At this time the Government offers Government Exhibit 31 for identification into evidence as Government Exhibit 31.

Mr. Bender: No objection.

(Government Exhibit 31 was received in evidence.)

Q. Handing the witness Government Exhibit 32 for identification, 33A through Y for identification, 35 for identification, 36A through D for identification, 37A through C for identification, 38A and B for identification as well as Government Exhibit 39 for identification, and going back to them one by one and in order, would you please identify them? A. Government Exhibit 32 is a stock receipt form of the Bankers Trust Company dated December 19, 1972, and it says that we have received 175,000 shares of General Investment Corporation stock registered in the name of Tri-State Energy, Inc., and it is for collateral for a loan.

Q. And was there a time that Bankers Trust in fact received such shares of General Investment Corporation as collateral for Tri-State? A. Yes, it would have been on or about December [295] 19, 1972.

Q. And the next exhibit? A. The next exhibit is Government Exhibit 33A through Y, and they represent shares of stock of General Investment Corporation registered in the name of Tri-State Energy, Inc.

Q. And to the best of your knowledge, are these the actual stock certificates that were received from Tri-State Energy? A. Yes, they were.

Q. And the next exhibit, please. A. Government Exhibit 34 is a stock receipt form of Bankers Trust indicating that we have as collateral 50,000 shares of Satellite

Systems Corp. from Tri-State Energy, Inc., and it is collateral for a loan.

Q. Do you recall that such stock was in fact received by Bankers Trust as collateral? A. Yes, I do. It was either on or about January 19, 1973.

Q. And the next exhibit. A. Government Exhibit 35 is a stock certificate of Satellite Systems Corporation representing 50,000 shares registered in the name of Tri-State Energy, Inc.

[296] Q. And to the best of your knowledge, is this the actual certificate that Bankers Trust received? A. Yes, it is.

Government's Exhibit 36A through D are stock certificates for Marlin Investment Company registered in the name of Bachelor Investments and they represent 20 thousand shares of the stock.

Q. And to the best of your knowledge, are those actual certificates which were received? A. Yes, they are.

Q. And the next exhibit. A. The next exhibit, which is Exhibit 37A through C, are stock powers signed by Bachelor Investment and guaranteed by the Chemical Bank.

Q. Did Bankers Trust receive those documents from representatives of Tri-State? A. Yes, they did.

Q. Can you recall in connection with what stock that was? A. It would have been in connection with the Marlin Investment stock.

Q. And the next exhibit. A. Government's Exhibit 38A is a letter of consent to pledge and hypothecate securities signed by Bachelor [297] Investments in favor of Tri-State Energy, Inc.

Q. And 38B? A. 38B is a form of the General Stock Transfer Company.

Q. Do you recall whether Bankers Trust had communication with General Stock Transfer about any of this collateral? A. Yes. The Bankers Trust has attempted to get the collateral registered in the name of Tri-State Energy, Inc. because when we had received the stock as collateral we had been told that this stock was really Tri-State Energy stock and that it should be registered in their name and this form is the result of the bank's attempts to register the stock in Tri-State Energy's name.

Mr. Bender: If the witness is talking about someone who told him something somewhere without further identification, we would object to it and move that that answer be stricken.

The Court: Do you recall by whom you were told?

The Witness: Rubin or Deaton or both of them.

Q. And to what stock were you referring? A. This is in connection with the Marlin Investment stock.

Q. And then this document, 38B was received from [298] General Stock Transfer by Bankers Trust Company? A. Yes.

Q. And was it the normal course of Bankers Trust's business to receive such documents? A. Yes, if you attempted to get a stock re-registered and for some reason it couldn't be re-registered, this would be the format for the reply.

Q. And this was received in the normal course of Bankers Trust's business? A. Yes, it was.

Q. And Government's Exhibit 39 for identification? A. Government's Exhibit 39 is a form dated January 30, 1973 and it is a form of Bankers Trust that is used when

stocks are going to be re-registered and basically it says that the bank is instructing that the 20 thousand shares of Marlin Investment Company be transferred and registered in the name of Tri-State Energy, Inc.

Q. Is this a photocopy of the actual bank form? A. Yes, it is.

Ms. Neugarten: At this time the government offers Government's Exhibits 32 through 39 for identification, including in some instances subparts A through the letters previously indicated, in evidence, as the exhibits by those numbers.

[299] Mr. Bender: May I ask one question?

The Court: Yes.

Voir Dire examination by Mr. Bender:

Q. On Exhibit 38, Mr. Keating, I guess "A-B"—

Ms. Neugarten: A is the first page and B is the second page.

Q. How did you describe that document? A. 38A is a letter of consent to pledge and hypothecate collateral.

Q. Did that document also give the bank authority to sell it? A. Yes, it did.

Q. I wanted to make sure you weren't just limiting it to pledging and hypothecating.

Mr. Bender: Thank you, your Honor.

The Court: All right.

Mr. Bender: May I again ask another question?

The Court: Yes.

John Joseph Keating—for Government—Direct

By Mr. Bender:

Q. On Exhibit 34 for identification which you identified as a stock receipt where the bank received 50 thousand shares of Satellite Systems Corporation, there is some handwriting on the face of it, "From Benjamin." Do you [300] know who wrote that? A. No, I do not.

• • •

[305] Q. Directing your attention back to the Allstate stock, which I think is indicated by Government's Exhibits 25 through 27, do you recall when the bank received it as collateral? A. The bank received the stock as collateral on or about November 10, 1972.

Q. Did it remain as collateral when the other loans that were dated after November 10th were made by the bank to Tri-State Energy? A. This stock was collateral for each and every loan Tri-State took from the Bankers Trust.

Q. So it was not limited to the first loan? A. No, it was not.

Q. What led to the bank receiving Allstate stock as collateral? A. It was delivered to us by either Deaton or Rubin or both of them for the bank.

Q. Had there been any request for it? A. This was part of the overall conversations that we have had with Tri-State from the beginning of the transaction that we wanted to get good marketable collateral that was not restricted.

So, this was part of that conversation. This was the result of it.

[306] Q. Was it in response to it? A. Yes.

Q. Do you recall who brought that collateral? A. Deaton or Rubin or both of them.

Q. Do you personally recall being told how Tri-State had obtained the Allstate stock which it was pledging as collateral? A. Yes.

Mr. Bender: May we have the conversation, your Honor, if there was a conversation, and with whom and when?

The Court: All right.

A. I recall in conversations with Deaton and Rubin that Tri-State had sold coal rights in their mine to this company so that they could get the stock as collateral.

Q. By "this company" do you mean Allstate? A. Yes.

Q. Were you told anything about the stock? A. That—

Q. And if so, by whom? A. We were told by Deaton or Rubin or both of them that the stock was in response to our request to get good marketable securities that was not restricted.

Q. Had you discussed the subject of collateral with [307] anyone from Tri-State before you received this Allstate stock? A. There were continuing conversations with Deaton and Rubin that we wanted to get not unrestricted stock, that our preference was to get New York Stock Exchange collateral, and we were promised on several occasions that we would be receiving unrestricted and New York Stock Exchange collateral.

Q. About how frequently before November 10th had you discussed this matter? A. Daily.

Q. With whom? A. With Deaton and Rubin.

Q. Did there come a time that you received stock of Management Dynamics as collateral? A. Yes.

Q. When again was that? A. (No response.)

Q. Is there a document you are looking for? A. Yes,

it is a stock receipt certificate which would have the date.

Q. If you look at Government's Exhibit 31. A. We received the stock of Management Dynamics on or about December 6, 1972.

[308] Q. And from whom did Bankers Trust receive it? A. Deaton or Rubin or both of them.

Q. Were you told anything by Rubin or Deaton about Management Dynamics?

> Mr. Bender: May we have, instead of leading, whether there was any conversation, with whom and when?
>
> The Court: All right.

A. On or about December 6, 1972 I had conversations with Deaton or Rubin or both of them, and again this was a—these conversations were continuous. You have to understand what was happening here. The people were coming into the bank almost on a daily basis, each time they would come in they would be describing various activities of the coal company and the conversations always evolved to the point of the collateral that we were holding and our desires to get New York Stock Exchange collateral.

This was presented to us, and actually it was not New York Stock Exchange collateral, it was our understanding that this collateral was marketable and it was not restricted.

Q. Were you told that? A. Yes.

Q. Did there come a time after you received Management Dynamics that you had another conversation [309] concerning it? A. Yes. I believe the date was December 15, 1972. Rubin came into the bank. It was a Friday afternoon and he indicated that they were going to swap

some coal rights and Management Dynamics stock, they meaning Tri-State Energy, for New York Stock Exchange collateral.

He wanted the stock released to him so that he could effect the swap. I didn't have the authority to make the withdrawal of the stock then and give it to Rubin. I went over to Ray Ludwig, I asked him for permission to release the stock. The permission was granted. I indicated to the general cage of the Seventh Avenue office that the stock was to be released and it was given to Rubin.

Q. Did Mr. Rubin tell you anything about his future intentions? A. Yes, he said that by Monday morning we would have New York Stock Exchange collateral in exchange.

Q. What day of the week was this conversation? A. It was a Friday.

Q. Did you receive anything from Mr. Rubin that following Monday? A. I received nothing at all.

Q. Do you recall talking to him that day? A. I don't recall specific conversations with him.

[310] Q. Did there come a time that you did talk to him again? A. I believe it was the following Wednesday. Rubin came into the bank and we received additional stock, but it was not New York Stock Exchange collateral. He indicated that the stock was marketable, that it wasn't restricted, that something had gone through with or fell through with the transaction that they were going to have with this unnamed stock exchange company, and that they had managed to get this other collateral, this other stock, in exchange for it.

Q. What was this other stock that you received? A. There would be a document—Satellite Systems Corporation stock.

Q. What is the date of that receipt? A. 1/19/73.

Q. I will check that. That's not correct. It would have been December 19, 1972 collateral, not the January, because it was December when he came into the bank. It was the General Investment Corporation's stock. It was 17,500 shares.

Q. What document is it that you are looking at to refresh your recollection? A. Government's Exhibit 32. It is a stock receipt [311] certificate dated the 19th of December.

Q. It was the General Investment stock that Mr. Rubin discussed that Wednesday? A. Yes.

Q. Did you make any response to Mr. Rubin? A. I was quite disturbed because I felt that it was a breach of confidence, that we were promised certain things and it just didn't transpire.

Q. Did you tell him that? A. Yes.

Q. Going back to that Satellite Systems that you just had there, did there come a time that you did in fact receive Satellite Systems? A. Yes. On January 19, 1973, on or about that date, we received 50,000 shares of Satellite Systems Corporation stock.

Q. Do you recell from whom you received it? A. It was either from Deaton or Rubin, I'm not sure which one.

Q. Did you ever receive any literature concerning it? A. Yes. Subsequent to this date, Deaton brought into the bank a clipping, a copy of a newspaper clipping from the International Herald Tribune, and the clipping was [312] a reflection of stock prices for a particular day, and circled on the clipping from the International Stock Exchange was bid and asked quotes of the Satellite Systems Corporation stock, stating that it was selling for approximately $20 a share.

Q. When you say "bid and asked," what do you mean? A. Well, on an over-the-counter security, there is two

prices, what somebody is—there is not the usual marketing in the New York Stock Exchange and a particular company or brokerage house, at least in the United States —I don't know how it works over in Europe—would make a market in the stock.

They would offer it at a certain price and somebody else might bid at it at a certain price.

Q. When Satellite Systems was brought in, did you have any conversation with the person who brought it to you? A. Yes. When the stock was brought into the bank, and I don't know who brought it in, it was Deaton or Rubin, the gentleman bringing it in was very happy saying, "Here is a stock, now you don't have to be asking all the time for New York Stock Exchange collateral, because while this isn't New York Stock Exchange collateral, here is collateral for you that is worth $1 million because we are at 50,000 shares, $20 a share."

[313] He says, "This stuff is readily marketable, it it not restricted, all the requests that you have should be more than satisfied by this particular piece of stock."

Q. Were you told how that Satellite Systems stock had been obtained? A. Yes, it was the same as each of the other pieces of collateral that we had received, and that was through the sale of coal rights to the mine that they owned in Kentucky.

Q. From whom did you receive the Marlin Investment Company stock? A. Deaton or Rubin or both of them, I can't recall.

Q. When you received it, were you told anything by the person from whom you received it? A. Yes. The Marlin Investment Company stock was registered in the name of Bachelor Investment Company. When the stock was presented to the bank, we had the pledge of stock

and hypothecation delivered with it, plus stock powers in the name of Bachelor Investment.

However, I was told that this particular stock was really Tri-State's property, and that we would be—we should register it in Tri-State's name because, again, Tri-State had obtained the stock through the sale of coal rights to this Bachelor Investment Company.

Q. So this hypothecation document which is 38A [314] there, what was its significance, what was its purpose? A. The purpose of the document was to give the bank the right to sell in between the time that we would take the stock in and when we would have it registered in Tri-State's name. In the event that we didn't have that document, then the stock would be worthless to us because there was nothing that would tie Bachelor Investment to the Tri-State loan.

Q. Were all of the discussions personal, face to face discussions with Rubin or Deaton held at Bankers Trust? A. No. There were a number of meetings that were held in the offices of Tri-State Energy.

Q. Did you go to Tri-State Energy by yourself or with anyone else? A. I went by myself once and I went with Ray Ludwig once.

Q. Do you recall whom from Tri-State was present? A. I recall meeting with Rubin and Deaton.

Q. Do you recall in whose office? A. I was in Rubin's office, and I believe I was in Deaton's office also.

Q. Do you recall when these meetings were? A. I'm not sure of the exact date, but I know it could be somewhere in the December to January time frame [315] basically because Rubin's office had all Christmas cards that he had received strung up on the wall on some string.

Q. Did you ever see them face to face anywhere other than their offices or your offices? A. I had lunch with them both, I know, on one occasion, that was some time, I believe, in October or early November, them meaning Rubin and Deaton.

* * *

[332] Q. Did the bank generate internal documents regarding Tri-State as well? A. Yes, all correspondence or any written information received from a client was gathered and maintained in the credit file.

Q. How was the credit file actually physically put together? A. It was a binder. Any documentation that would come into the bank would have holes punched in it and attached to clips inside the binder.

Q. And it was the normal course of business for Bankers Trust to compose a credit file about a loan account? A. Any correspondence coming in on any borrowing account or commercial account would have a credit file.

Q. And the one that was made in this case, that is the Tri-State Energy credit file, that was made in the normal course of Bankers Trust business? A. Yes, it was.

* * *

[335] Q. Handing you a pasteboard bound folder, two sides, left and right, marked in toto Government Exhibit 49 for identification, do you recognize this compilation of documents? A. Yes. This is the credit file for Tri-State Energy Incorporated.

Q. Before coming to court today have you at some point coded or paginated the various documents in there? A. Yes, I have.

Q. Will you explain how you did that? A. I coded everything on the left side of the credit file A, numbered 1 through whatever the end is, and on the right side of the credit file was numbered B- and numbers going out after that.

[336] Q. And your sequential numbering system, for instance, on this right side document, B-1 is the top document and the numbers get higher as you get to the bottom of the folder, is that correct? A. Yes. It goes from B-1 to B-58.

Q. And on the left side here we start with document A-1 and go sequentially with the higher numbers at the bottom of the folder, correct? A. Yes, it goes to A-44.

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[338] The Court: 49 is received.

(Government Exhibit 49 was received in evidence.)

The Court. Let's proceed.

Q. Now, as I ask you questions about this document, I am going to refer to numbers according to your coded page numbers. When responding if you would also refer to the coded page numbers for purposes of the record, and so we all know where we are going— A. Okay.

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[339] Q. Directing your attention to document B-2A and also to B-3A, describe what B-2A is and hold it up to the jury. A. B-2A is the financial statement of Tri-State [340] Energy dated October 20, 1972, and it is prepared by Englander & Bernstein, CPA's.

Q. That is two pages, B2-A followed by B2-B and that is a report? A. And 2C.

Q. And 2C then is what? A. It is the balance sheet of the financial statement. B-2A and B-2B are notes to the financial statement.

Q. And B-2A and 2B are signed by Englander & Bernstein? A. Yes.

Q. And the date of the balance sheet? A. October 20, 1972.

Q. And the date of the report? A. The date of the report is October 20, 1972.

* * *

[353] Q. Turning to document B11A. A. Document B11A is a projection that was presented to us by Tri-State Energy, Inc.

Q. By whom? A. That I can't recall. It would have been Deaton or Rubin or perhaps both of them. The Tri-State Energy, Inc. projection shows the revenues that could be gathered predicated on different daily gross tonnages of coal which would be mined from the operation, and the projection covers the revenue, profit and capital expenditures which would be associated with each of the various assumptions.

Q. What significance, if any, did that document have to you? A. Well, just basically outlined that given the amount of coal that Tri-State Energy, that they could generate a substantial profit from their operations under a number of different alternatives, starting with 500,000 tons or 500 tons a day, up to 5,300 tons a day.

Q. Document B—strike that.

About when did you receive this projection? A. It would have been on or about the same time that the balance sheet was presented to us.

John Joseph Keating—for Government—Direct

Q. You testified that was October 27th? [354] A. Yes.

Q. Document B45? A. Document B45 is a map that was presented to us by Tri-State of their coal mine.

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[355] Q. What were you told? A. That it was a subsidiary of Tri-State Energy and that they had tremendous reserves of natural gas located in Tennessee.

Q. Did they quantify those reserves in any way? A. Yes.

There was an outline or synopsis that was presented to us. I believe there were 330 billion cubic feet of natural gas with a recoverable value of $250 million.

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Q. Directing your attention to Document B7. A. Document B7 is a letter from American Leisure Corporation to William R. Rubin dated October 27, 1972 signed by Jack Lipschitz, President.

Q. Do you recall how you got this letter? A. Yes, it was presented to us by Rubin or Deaton or both of them.

Q. Do you recall approximately when? A. It would have been in late October, early November 1972.

Q. Did you discuss it with anyone? [356] A. Yes, I discussed it with Mr. Rubin.

Q. What was the substance of that conversation? A. Well, it was in connection with the American Leisure Corporation stock of 400,000 shares that we had received when the loan was first put on. Mr. Rubin had indicated that the shares—that the restriction, the stamp that was on the face of the shares would be removed at some future date, and basically the letter was demonstrating that this was going to happen.

Q. Did that ever happen? A. No, it did not.

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[365] Q. Turning to document A-19. A. Document A-19 is a projection that was prepared by Mr. Rubin and delivered to me by Mr. Rubin.

Q. How do you know it was prepared by Rubin? A. He told me he prepared it.

Q. About when did he deliver it to you? A. It was some time after the initial loan was made, October, late October, early November 1972.

Q. Did you have any discussions with him concerning it? A. Yes. This was the—as far as I was concerned, this was one of the most important documents that I had received from the company. What it did is it gave me an analysis of when the company was going to generate cash from the sale of coal and how much was going to be generated and when the—what the cash would be used for and what the net figure or net cash flow of the company [366] was so that that could be used to retire any bank loans that had been made.

Now, the document indicates that sales would be made of $120,000 in December 1972, 240 in January of 1973, and 180 in February of 1973.

Now, the sales that are associated with this were $300,000 from a Continental Coal Corporation and $240,000 from Repoca Resources.

Q. How is that indicated on the document? A. I've got notes on the document which indicate that.

Q. What are those notes, if you would read them? A. Three hundred thousand or three hundred "M" which means thousand, C/C/C, 240,000 R/R.

John Joseph Keating—for Government—Direct

Q. I take it C/C/C is Continental Coal? A. That's right.

Q. And R/R is Repoca Resources? A. That's correct.

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[370] Q. And I believe you had just explained what CCC and RR were. A. Right. As I stated, this was a projection which Rubin had prepared for us indicating how Tri-State was going to generate sufficient cash to pay off our loans and the projection indicated that $540,000 would be generated in the December 1972 to February 1973 period. There would be equipment purchases of approximately $200,000 for a net cash flow of $340,000. The way it was explained to me by Rubin, this was on a specific basis. In addition to this there were other items that were outstanding that may not necessarily happen at this particular [371] point. He wasn't putting it in his firm projection. But he did indicate that the firm had been in negotiations on other fronts besides just the sale of coal to these two companies, one of which was—he stated there would be $200,000 received through down payments for the sale of gas in place in Tennessee, and the institution of driling programs for the exploration of reserves in Scott and Morgan Counties, Tennessee.

He stated that this particular money will be coming from a company called Ohio Gas.

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A. And the last part of the projection, that outlines that it is the opinion of the management that the cash flow generated from operations through February 1973 will be more than sufficient to meet a monthly [372] amortization schedule of $100,000 per month.

John Joseph Keating—for Government—Direct

In addition to the information that I already stated there is a mention in the projection of a long term export contract from Roland-Werkstatten, which was a German company that wanted to import coal from Tri-State Energy.

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[375] Q. Continuing with Document A9, what if any [376] significance had this document to you as a lending officer? A. At that time this was the most significant document that I had received. When we made the loan to Tri-State we made the loan with the overall operations of Tri-State; the sale of coal, the sale of natural gas being their business.

This was how cash was going to be generated to repay the loan. This was our primary source of repayment and this document indicated to us what, how and when they were going to repay the loan.

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[378] Q. Directing your attention to Document A18. A. Document A18 is a Dun & Bradstreet report on Tri-State Energy, Inc. and it is dated November 30, 1972.

Q. How did it come to be in the credit file? A. It was ordered on the corporation. It was standard policy to order something like this on an account.

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[379] Q. Turning to document B47A. B47A is a description of the lease on the coal properties in Kentucky.

Q. How did you come to have it. A. This was presented to me by Rubin, Deaton or both.

John Joseph Keating—for Government—Direct

Q. Do you recall if you had any discussion concerning it? A. Well, I had discussions. As far as the substance of the exact conversation, I can't recall. Basically it was an indication of overall strength of the company, how much coal they had, and an outline of where the operations were.

[380] Q. Turning your attention to page 47C, which is to say B47C of that document. A. Yes.

Q. Do you see a summary? A. Yes. The summary indicates that—

Q. Could you, rather than summarize it, would you read it to the jury? A. "In summary, the three major seams, the Amburgy, the Whitesburg and the Hazard 4, are all high range coals with low sulfur and high BTU characteristics. These traits make the coal especially attractive to metalurgical coking markets, and the low sulfur can demand a premium price in the increasingly pollution conscious steam market of the north. The three other seams, the Hazard 5A, the Amburgy Rider and the Elkhorn 3 are not calculated as part of the reserves. Rather, they serve as a compensatory factor to allow for error in the calculations of the other reserves."

Q. Directing your attention to page 47E, that is B47E of that document, do you see an indication at the bottom, a statement of the total reserves? A. 24,070,547.

Q. Looking again to page 47F, do you see a figure for total reserves? A. Yes, 24,070,547.

[381] Q. Turning to page 48B, do you see a description of the Whitesburg seam? A. Yes.

Q. Would you read the first paragraph of that description? A. "Thickness ranging from 30 to 45 in avergaging 36 inches. The Whitesburg coal is good metalurgical coal and high grade blending steam coal. It is an analysis"—

Q. And then read the numbers. A. BTU 13,500.8 per-

cent maximum, around 8 percent, fixed carbon 52.2 percent, vol. matters 35.2 percent, FSI 5.

Q. Turning to page B50. A. B50 is a letter from Otto E. Sebold to Tri-State Energy dated September 20, 1972.

Q. Does it state the present value of certain coal? A. Yes. He states that it is his opinion that the present value of the coal is $3 per ton in place.

Q. That price, $3 a ton in place, do you recall whether that is the same or different as you discussed with respect to that October 20th balance sheet? A. Same amount.

* * *

[382] Directing your attention to B48A, B and C, as well as B50. A. All right.

Q. Did you have any discussion concerning those documents? A. Yes. We had discussions on the size of the reserve, the strengths. My basic impression, after the discussions and the discussions would have been with Rubin or Deaton or both of them, I don't recall, is that the Tri-State Energy had tremendous reserves of coal. Most of [383] these reports added to—we are given as substance that they did have good reserves of coal and that's the basic outline in what these documents contained.

Q. Directing your attention to document B29. A. Document B29, it appears to be a letter from Continental Coal Corporation to Tri-State Energy, Inc. dated December 14, 1972.

Q. How did you come to have that? A. It was given to me by Rubin, Deaton or both.

Q. Did you have any discussions concerning this? A. Yes. This was presented as further authenticity of the projections that had been presented to us previously. The letter speaks about buying coal at $9.25 per ton. This was

just further verification that the sales that were indicated in those projections were going to materialize.

Q. Directing your attention to document B28, the back side of that document. A. B28 is a copy of a cable or a Telex to Mr. Deaton from Ian J. Ward.

Q. Are you referring to the front, back or both of B28? A. I am referring to the back. The date of the cable is December 13, 1972 and the cable states that, "This will confirm our interest in purchasing approximately 750 [384] short tons per day of your Neon Kentucky Coking Coal per your analysis of September 5, 1972. It is my understanding that you require U.S. dollars 12, per short ton loaded on rail cars at Neon. I am awaiting confirmation of rail rates and loading facilities and will revert to you as soon as possible."

Q. Do you recall how you got document B28? A. It was delivered to me by Rubin or Deaton or both of them.

Q. Do you recall when? A. It would have been in December or January, December 1972 or January of 1973.

Q. Did you have any conversation regarding that? A. Yes. It was just, again, a further indication of the overall story we had been receiving that the coal was going to be sold.

Q. Documents B52, B53, B54 and B55. A. Document B52 is a letter from Rapoca Resources to C. W. Deaton, Tri-State Energy Corporation, dated November 28, 1972. The letter states that "We are pleased to submit the following purchase bid on our coal located at Neon, Kentucky. $12 per ton, 20,000 tons graded 2 in-0 in loaded in car at Neon, Kentucky per analysis of Standard Laboratories, Inc. Delivery of the above tonnage to begin [385] no later than January 15, 1973."

Q. And B54 and 55? A. B54 is a domestic bank checking on Rapoca Resources, Inc., and it is dated November

29, 1972. It was done with the 53rd Bank. It doesn't say where the bank was located, but the checking outlines the borrowings that they were—that that bank was loaning to Rapoca Resources. It indicated that it probably was a substantial company because they were loaning them $400 thousand unsecured and 3.5 million dollars secured.

Q. Does the document indicate the reason for this bank check? A. It says "Bankers Trust Company has been asked to lend against a commitment from subject."

Q. From that, what do you understand to be the reason? A. From the analysis here is that we were probably approached to lend against the actual sale of coal that would be transmitted between Tri-State Energy and Rapoca Resources.

Q. Directing your attention to document B23. A. Document B23 is a letter from a German company, Roland-Werkstatten, to Tri-State Energy, Inc. to the attention of Leonard James, dated December 3, 1972.

[386] Q. Do you recall how you obtained this document? A. It was presented to me by Rubin, or Deaton, or both of them.

Q. Is that the same company that is mentioned in the projection you discussed earlier? A. Yes, it is.

Q. Did you have any discussions concerning this document B23? A. Yes. Tri-State was going to sell the German company coal, and the method of sale was to be by a letter of credit. A letter of credit is basically an instrument that facilitates international trade.

* * *

[389] Q. Directing your attention to document A11A, through A12. A. These documents concern a proposal of

natural gas [390] sales to Anheuser Busch. Where did you say to end off on?

Q. Through A12. A. It is just an analysis of what they could make and how much gas Anheuser Busch would be using.

Q. How did you come to get these documents? A. These were delivered by Rubin or Deaton or both of them.

Q. Did you have any discussion concerning this transaction? A. Yes, it was again part of the overall, the other prong approach of Tri-State Energy. It was one hand coal, the other part natural gas, and this particular document was used as an example of what plants they had, who they were talking to and again, as a further instance of how they would be able to generate cash to repay loans.

[391] Q. Do you recall being told anything about the transaction with Anheuser-Busch? A. Yes. Apparently the General Oil & Gas who was the subsidiary of Tri-State, who owned the natural gas fields in Tennessee,—and I am not sure of the exact terminology at this time—it's either that fields were dedicated or they were not dedicated. It had something to do with that. Basically Anheuser-Busch, if they bought the gas from General Oil & Gas, they could buy it cheaper than from other sources. So it would be a good deal for Anheuser-Busch and a good deal for Tri-State.

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[395] Q. Handing you Government Exhibit 47 in evidence, does it contain any information regarding General Oil & Gas? A. Yes, it states that "General Oil & Gas is a subsidiary of Tri-State Energy and it has approxi-

mately 330 billion cubic feet of natural gas which, at today's prices, would have a recoverable value of $250 million."

* * *

[396] A. Yes.

Q. Advancing to the next paragraph, the third full paragraph on the first page, would you read the first and second sentence? A. "We have advanced 475,000 on paper submitted by 750 in marketable securities as lien collateral. In the near future, we expect the lien collateral to be replaced by guaranteed letter of credit which will be opened in our favor to support the loan."

Q. I believe you testified earlier that there was a time when a series of bounced checks or overdrafts were experienced in the Tri-State account. A. Yes.

Q. Did you discuss those bounced checks with anyone? A. Yes, I discussed it with Rubin on several occasions.

* * *

Q. Do you recall the substance of those conversations? A. Yes, I kept on telling Rubin that it was [397] senseless to be sending out checks if he didn't have any money in the bank because I wasn't going to pay them. He indicated that Deaton had the checkbook, Deaton was writing all of the checks and that he was really unable to control him.

* * *

[403] Q. Directing your attention back to the credit file, to page B22 and B24. A. B22 is a letter from C. W. Deaton to Onyx Investment Limited in Montreal, dated January 20, 1973.

B24 is a listing of mining equipment.

John Joseph Keating—for Government—Direct

Q. Do you recall what these documents—first of all, do you recall how you obtained these documents? A. They were delivered to me by Rubin or Deaton or both of them.

The documents were in connection with a loan that Tri-State was trying to get from Onyx Investments Limited, and the loan was for $2.25 million, and it would cover the purchase of mining equipment, plus working capital for the company.

[404] Q. And did you discuss this letter with anyone? A. Yes, I discussed it with Rubin or Deaton or both of them.

Q. What relation, if any, did the document B24 have to the letter B22? A. That was the equipment listing that the loan was covering.

Q. And this is the same company from which you had received an inquiry, you earlier testified? A. Yes.

Q. And were you told how this equipment was to be paid for? A. Yes, the loan basically was to be gotten by, again, a swap of coal and this was the standard practice that Tri-State had used to get the securities or the stocks that we had as collateral and it was also part and parcel of this particular transaction.

Q. Did you have any reaction to Tri-State's suggestions that it was swapping its coal reserves? A. I figured that they had plenty of coal, that it was better to get cash than to sit on reserves, the theory being that half a pie was better than a whole pie if you weren't going to get anything.

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[410] Q. Directing your attention to document B58. A. This is a copy of a newspaper article from the International Herald Tribune dated January 22, 1973.

Q. How did the bank come to have this copy? A. Deaton brought it into the bank. Basically, it was an indication that the Satellite Systems Corporation stock that had been brought or given to the bank as collateral [411] was in fact trading at 20 to 20.50 dollars a share as indicated in the newspaper clipping.

Q. Directing your attention to Document A7. A. A7 is a memo from me to William Powderly dated February 2, 1973. The document indicates that "Pursuant to a phone conversation with Ray Ludwig, the following is a list of the side collateral which we have in support of our loan to the subject," meaning Tri-State Energy.

Q. Do you recall what occasioned your sending this memorandum? A. Not specifically.

I know there was a conversation with Powderly on the account and, you know, from Ludwig, he wanted Powderly to know what collateral we had and which of the collateral was restricted and which was marketable.

Q. Who was Mr. Powderly? A. He was vice president in Loan Administration who had concurrent responsibility for the office above a half million dollars.

Q. On an organizational chart, what relationship did he bear to Mr. Ludwig? A. He was his superior for credit purposes.

Q. And for credit purposes, would include loans; is that correct? [412] A. Loans, right.

Q. And Document A2? A. Document A2 is a memo from Bill Powderly to me dated February 5, 1973 on Tri-State Energy, Inc. and the memo asks, "With respect to the stock collateral we hold, do we have complete documentation including our standard form of resolution for transfer of each issue? Please check this with Mr. Miller and send me a short memo."

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Q. Directing your attention to Document B38. A. Document B38 is a checking that was performed on All States Life Insurance Company, dated February 6, 1973.

Q. And that is an internal bank document? A. Yes, it is.

Q. Does it indicate for whom this checking was performed? [413] A. It was requested by me.

Q. Your initials are on it? A. Yes.

Q. How did they come to get there? A. I signed it.

You know, I don't recall specifically what caused me to get this particular investigation performed, but it was performed. I don't know what instituted it.

Q. And when the document reflecting the checking was completed, it was sent to you and you initialed it? A. Yes.

Q. Is that true for B39? A. Yes.

Q. And the date at the top? A. February 6, 1973, checking on General Investment Corporation.

Q. What date does that reflect? A. That would be the date that the investigation was either made or typed out.

Q. And document B51? A. B51 is an investigation on Marlin Investment Company dated February 6, 1973.

Q. Is it again requested by you? A. Yes.

[414] Q. As indicated by your initials? A. Yes.

Q. And document B35B. A. B35B is a checking on American Leisure Corporation dated February 6, 1973, and it again contains my initials.

Q. And 35A? A. 35A is a bank checking on American Leisure Corporation dated January 16, '73 and it was requested by Mr. Ludwig and me and it indicates no accounts with the exception of a closed account at Chemical Bank.

Q. Directing your attention to document A44. A. A44 is a letter dated February 7, 1973 from me to the International Stock Exchange in London asking for information that might be available on the stock of Satellite Systems Corporation, including the current trading price and whether or not it is actively traded.

Q. And what date does that bear? A. February 7, 1973.

Q. This series of checkings, both on the bank forms and your letter, was there a reason why you requested them or did them? A. Well, there was a reason. At this time I don't recall why I instituted the checkings. I have opinions on why I did. There were so many things going on at this [415] particular time.

Number one, it was—

> Mr. Bender: Your Honor, may we have an answer to the question, a responsive answer, rather than an exposition?
>
> (Question read.)

A. Yes, but I don't recall at this time why I instituted the checkings.

Q. Had you any concerns at this time? A. Yes, I did. At that time the account had been overdrawn. Many of the things that were indicated in the projections had not transpired. It was subsequent to this party that Ludwig was present at that certain information was stated that—

> Mr. Bender: I object to this. I knew we were going to try to get this in the back way, particularly after we had that side bar conference. That is why I objected.

The Court: Yes. You have not been able to testify as to what transpired at that party, so please do not refer to it.

A. Many things were happening that were of concern to me at that time and all of the things which I had stated and basically the lack of performance to date by the company in meeting its projections.

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[419] Q. Directing your attention to Government's—the credit file, page A25. A. A25 is a request for a D & B report on general [420] investment dated February 9, 1973.

Q. By D & B, do you mean Dun & Bradstreet? A. Dun & Bradstreet.

Q. For A35, what is that? A. A35 is a request for Dun & Bradstreet report on Sagor Corporation.

Q. And A32? A. A32 is a Dun & Bradstreet Report on [Marlin] Investment Co. dated February 12, 1973.

Q. The A36? A. A36 is a request for a Dun & Bradstreet report on Satellite Systems Corporation dated February 12, 1973.

Q. No that's the date of the request, is that correct? A. Right.

Q. Then A37? A. A37 is the Dun & Bradstreet report on Satellite Systems Corporation dated February 12, 1973.

Q. Now, both [Marlin] Investment Co., the subject of A32, and Satellite, those were companies whose stock was collateral for this loan? A. Yes, it was.

Q. Did there come a time that you received, you individually received the Dun & Bradstreet on Satellite, [421] document A37? A. Yes.

Q. Do you recall about when you received it? A. February or March, 1973.

Q. Did you do anything in response to it? A. Yes. After receiving the report, I called a Mr. Benjamin who was listed in the report as a principal of the corporation.

Q. In response to your call with Mr. Benjamin—strike that.

Did you have a conversation with Mr. Benjamin? A. I had a conversation with Mr. Benjamin.

Q. Then in response to that conversation with Mr. Benjamin, did you do anything? A. Yes, I called Mr. Rubin.

Q. Did you have a conversation with Mr. Rubin? A. Yes. The substance of the conversation with Mr. Rubin basically revolved around the conversation which I had with Mr. Benjamin.

Q. Can you tell us what you told Mr. Rubin as you recall it and what Mr. Rubin told you? A. I told Mr. Rubin that Mr. Benjamin had said that this stock on Satellite Systems Corporation was restricted stock. There was an investment letter attached to the stock [422] and that it could not be used as collateral for any loan. Mr. Rubin told me that that is crazy, that's been defrauded because they had traded coal rights for the Satellite Systems stock, and that he was going to have his attorney look into the matter.

Q. Did you ever meet a William Hamilton? A. Yes, I did.

Q. With whom did you meet Mr. Hamilton? A. I met Mr. Hamilton with Mr. Rubin in the branch at 550 Seventh Avenue.

Q. That is the Bankers Trust Branch? A. Yes.

Q. Do you recall when that was? A. It would have been in January or February somewhere in that area of 1973. I am not certain of the exact time.

Q. Do you recall what conversation you had with Mr. Rubin and Hamilton? A. Yes. I had a conversation with both of them and I am not sure exactly what stock it resolved around. It either was in reference to the Marlin Investment Co. stock or it was in reference to Satellite System. At this time, I am not sure which one it was in reference to.

Q. But it was one of the two? [423] A. Yes, but the substance of the conversation was that Mr. Hamilton represented himself as being the attorney for Tri-State Energy and that he indicated that they had been defrauded by either Bachelor Investments or by Benjamin of Satellite Systems because they had traded stock and they did not have any knowledge that any of this stock was restricted and that it was crazy. He was going to institute a lawsuit.

Q. Directing your attention to documents A26 and 27. A. A26 is a request for a Dun & Bradstreet on Charter Financial Limited dated February 12, 1972 and A27 is a letter dated February 8—1973, the date of the Charter Financial request for Dun & Bradstreet. It should be 2/12/73. Document A27 is a letter to the manager of Barclay's Bank, 120 Broadway, New York, dated February 8, 1973, initialed by me asking for information on Charter Financial Limited.

Q. Document A24? A. Document A25 is a Dun & Bradstreet report on American Leisure Corporation dated February 13, 1973.

Q. And document A4? A. Document A4 is a memorandum dated February 22, 1973 from me to Emanuel Miller, Associate General Counsel of [424] Bankers Trust on Tri-State Energy. The substance of the memo asks that for him to examine contracts covering the mineral

royalty rights of the subject firm on properties in Kentucky, it's to see if we could take an assignment and use the mineral royalty rights as collateral for our loan.

[425] Q. Is there anything attached to that memorandum? A. It is documents A5A and 5B and 5C and 5D, 5E, 5F and 5G, which is basically a copy of the rights that Tri-State had to the coal properties.

Q. Now, how would you have gotten these attachments, that is the copies of the rights to the coal properties. A. It was given to me by Rubin or Deaton or both of them. Q. There came a time when a demand note was executed, is that correct? A. That's correct.

Q. That was February 26, 1973? A. That's right.

Q. At that time, what were the options that you and Mr. Ludwig had with respect to this loan? A. We would call the loan at that time, we could let it—there were, I believe, two notes that had already matured, that had come due, and there were two notes that had yet to mature. We could just let the notes be carried on a past due basis and wait for whatever events to happen, or we could take everything and put it into one neat package, that is the demand note so that there would be one instrument of debt representing all of the $475 thousand in loans.

Q. And was there a reason for making the choice [426] you did? A. Normally that was the policy of the bank, when there was a problem loan to put it on a demand basis.

Q. At that time, had you any expectation regarding whether or not the note would be repaid? A. I still thought that the loan would be repaid.

Q. Why was that? A. Well, from conversations at that time when the note was signed with James, and

those conversations reverted around several factors that he had brought to my attention on that day.

Number one, he said that there was a coal strike in Kentucky, that there was coal in sidings in cars at the—waiting to be shipped. He indicated that they were approaching the Bank of New York and First National City Bank's mineral group to seek out a loan.

In addition to that, they were looking for an SBA loan from some bank in New Jersey. It was just the litany of events that were described to me which indicated that, yes, they were having problems, but they would extricate themselves from the problems and repay the loan.

Q. And this was on February 26, 1973? A. Yes.

Q. Did he tell you anything about the coal in [427] Kentucky? A. He said that it was in side cars or railway cars that couldn't be shipped because there was a coal strike.

Mr. Bender: Excuse me, your Honor, I take it you are taking this subject to connection.

The Court: Yes.

Mr. Bender: As far as Rubin is concerned.

Q. When was the last time you saw Mr. James? A. That day, until today or—

Q. Have you seen him today? A. Yes. He was in the courtroom.

Q. Have you seen him anywhere else today? A. He was in the hall speaking to Mr. Rubin.

Q. Directing your attention to document B16. A. 16 is a subpoena from the United States Department of—not a subpoena, an inquiry from the United States De-

partment of Justice, dated February 23, 1973 asking for information on Intercommunications Systems, Inc. North American Mutual Funds, Tri-State Energy Company and C. W. Deaton, and the inquiry was received by Bankers Trust Company.

There is a time stamp on it on February 28, 1973.

Q. So that was two days after the demand note? [428] A. Yes.

Q. Directing your attention to document A1. A. A1 is a demand letter that was sent to Mr. Leonard James on March 5, 1973 with copies to Mr. James, Mr. Deaton and Mr. Rubin. The document states that "This will serve as your notice that unless our demand note for $475 thousand dated February 26, 1973 is repaid in full within three business days of the date of this letter, we will commence selling the collateral we hold without any further separate notice."

Q. Do you recall whether there was any response to this letter? A. No, I don't recall.

Q. Does it indicate carbon copies were sent? A. Yes.

Q. To whom were they sent? A. Mr. James, Mr. Deaton and Mr. Rubin.

[429] Q. Why were carbon copies sent? A. Because they were the guarantors of the loan.

Q. To the best of your knowledge, was that loan repaid in full within three days? A. No, it was not.

Q. Do you know for certain it was not? A. For certain.

Q. To the best of your knowledge, has it ever been repaid? A. No. I believe it was charged off by the bank.

Q. Apart from these credit checks that you had performed in January and February of 1973, up to December 6, 1972, that is going back several months, had you done

any checkings with third parties, that is anyone other than the three people from Tri-State? A. Well, there were daily litigation checks on the individuals that were performed to find out if they were being sued by anybody.

Q. What was the result of that check? A. They came up clear.

Q. Did you do anything else? A. I don't believe that I did at that particular time.

Q. Did you pull Dun & Bradstreet on the company [430] itself? A. Dun & Bradstreet was pulled also as a matter of course by the credit department, so that would have been extra financial information that would be ordered. That didn't have to be done at my direction.

Q. Did you ever do any checking with regard to the accounting firm? A. Yes, the accounting firm was checked out also to find out what kind of accounts that they were auditing or doing work for within Bankers Trust or any of the other banks in New York City.

Q. This checking, rather the degree and extent of this checking, was this normal or abnormal in your experience? A. It wasn't abnormal because of the nature of how the account had come into the bank.

Q. What do you mean by that? A. Well, the account came to Ludwig, who was the branch manager, and he had known Rubin as an accountant with an accounting firm called Fred Landau & Company in the past. It was normal, under the circumstances, that if you had a very good reference and you were very, very familiar with the people that were involved in this thing, that you wouldn't do the amount of detective work [431] that you would if something just walked in the door.

Q. So was the checking for someone who was known to the bank different than if someone had walked in off the street asking for a car loan, say? A. Yes.

Q. And the reason? A. Because of our knowledge of the individual and respect for his judgment.

Q. To the best of your knowledge, had Mr. Rubin had prior dealings with the bank? A. Yes. He was known to Ludwig from his days as an accountant with Fred Landau & Company.

Q. Directing your attention to document B26-A. A. B26-A is a memorandum on Tri-State Energy Company describing their operation, both in the coal and in the natural gas areas.

Q. From whom did you get this document? A. This would have been received from Rubin or Deaton or both of them.

Q. Turning to the second page of this document, do you see a discussion of General Oil & Gas? A. Yes. There is an analysis of their operation with specific reference to the amount of natural gas that they had and the amount of dollars which they believed [432] could be recovered from the natural gas.

Q. Do you see a sentence in the middle of that second paragraph commencing "General also has"? A. Yes.

Q. Would you read that please, that sentence? A. "General also has leases and options to purchase the natural gas located under approximately 250,000 acres in Scott and Morgan Counties, Tennessee. Attached is a map showing all existing pipeline and gathering systems in the area in the proposed Morgan and Scott County System."

Q. Before that, do you see immediately before it a sentence with a certificate of convenience? A. Yes.

Q. Would you read that? A. Would you repeat that?

Q. The sentence immediately preceding the one you just read. A. "General received a certificate of convenience and necessity from the State of Tennessee to operate as a public utility in the transmission transportation and pur-

chase and sale of natural gas and byproducts thereof. Attached release from Public Service Commission."

Q. Directing your attention to document B31. [433] A. Document B31 is a copy of that Tennessee Public Service Commission announcement stating that "General Oil & Gas, Inc., CCN, to operators of public utility in the transmission, transportation and purchase and sale of natural gas and the byproducts thereof."

Q. Were you ever told anything else regarding this certificate of operation? A. No, I was not.

Q. Directing your attention to document B34-A. A. Document B34-A is a copy of a printed financial statement in writing of American Leisure Corporation and subsidiaries as of September 30, 1971.

Q. Do you know how you received this document? A. It would have been presented to us by Rubin or Deaton or both.

Q. Does that apply to the whole series which is B34-A through B34-E? A. Yes, it does. It is all part of the same financial statement.

Q. Document A31-A? A. A31-A is a Dun & Bradstreet report on Insurance Industries, Inc., dated July 26, 1972.

Q. Do you recall how you came to receive that? A. That was ordered by the bank, but I don't know [434] why it was done.

Q. Document B41-A. A. Document B41-A is a financial statement prepared by Dale W. Ogden, certified public accountant, on General Oil & Gas, Inc. as of July 31, 1972. The letter of transmittal is dated August 25, 1972.

Q. Do you know how you came to receive it? A. It would be delivered to the bank by Rubin or Deaton or both of them.

Q. Do you recall at what point? A. Early October, November, 1972.

John Joseph Keating—for Government—Cross

Q. Directing your attention to document A3. A. Document A3 is a subpoena from the United States District Court, Southern District of New York, directed to Bankers Trust Company and it was dated the 14th of March 1973, and it asks for all records, internal memoranda, correspondence and documents relating to any loans to Tri-State Energy Corporation for the years 1972 to the date hereof.

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(Cross Examination)

[480] Q. You testified that the first note reflected a loan of $50,000 from the bank? A. Yes.

Q. This actually was more or less an unsecured loan for the $50,000 wasn't it, based pretty much upon the favorable background that Mr. Rubin had with the bank? A. The note itself was an on-paper note.

Q. Excuse me, just answer the question. You will have a chance to explain later. I think we will get along further if you are responsive to the question. A. It was not an unsecured loan.

Q. Did you ever indicate that this first $50,000—did you ever indicate to any agent or any attorneys or anyone else that this was an unsecured loan for $50,000 where subsequently some security in the form of this restricted stock was given to support the events? A. I don't know what I said to agents. I do know that that note was signed on the 19th and on the 20th it was booked and when it was booked we had American Leisure stock. Therefore, the loan was not unsecured.

Q. Was the money given before the stock was received? A. The stock was received on the 20th of October and that is when the loan was made.

[481] Q. Is that your best recollection? A. To the best of my recollection.

Q. That is your best recollection, that you never said to anyone that the first note was unsecured but nevertheless the American Leisure restricted stock was then sent in to support the events? A. The loan was made with American Leisure stock as collateral for the loan.

Q. Could you tell us, looking at your credit file—maybe you can help us—is there anything here which indicates that the American Leisure stock was actually received by the bank on October 20?

Do you know without looking at that, sir, what the basis of your information is? A. The S.R. ticket which was one of the exhibits is dated the 20th of October, to the best of my recollection.

Q. Is that the only thing that you go on, the fact that it was dated October 20? A. Yes.

Q. But nothing else? You have no independent recollection of that? A. I have independent recollection also.

Q. What is that based on? A. That the loan was made secured by American [482] Leisure stock.

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[580] Q. Would you be good enough to tell us when the bank received American Leisure stock, according to the stock receipt? A. That one isn't here.

Q. I can't hear you? A. That one isn't here. I know there is one. I need the number. According to the stock receipt we received the American Leisure Corporation stock on or about 10/20/72.

Q. On or about what date, sir? A. 10/20/72.

Q. That was the stock receipt which is the form of stock certificate issued by the bank that you testified to before? A. This is the stock receipt ticket.

Q. That is exhibit— A. 10.

Q. When did you receive Allstate stock? That was [581] 1000 shares I think you testified, in the name of Tri-State and 1000 in the name of Albert Combs? A. Yes. This collateral was received on or about November 10, 1972.

Q. That certificate is what number? A. 24.

Q. When did you receive the General Investment stock? A. General Investment Corporation was received on or about December 19, 1972.

Q. That again is from the stock receipt which is Exhibit 31? A. 32.

Q. Excuse me. The stock receipt Exhibit 31 is the receipt of the stock of Management Dynamics? A. Yes, it is. That was received on December—on or about December 6, 1972.

Q. Exhibit 34 is the stock receipt, is it not, of the bank for the receipt of the Satellite Systems stock and that is dated January 19, 1973? A. Yes, it is.

Q. When was it, about what time you received the stock certificate of Marlin Investment? That is what you testified about this morning. A. It would have—I can't give you an exact date. [582] It would have been before January 30.

Q. You testified today it was some time in January, before January 30? A. That's right.

* * *

[Redirect Examination]

[591] Q. Addressing your attention to Government Exhibit 65, does it indicate collateral received on the Tri-State Energy loan? A. Yes, it does.

Q. Does it indicate dates next to that collateral? A. Yes, it does.

Q. What were those dates? What did you intend those dates to mean when you prepared that document? A. It would have been the dates that we received the stock.

Q. And was this document accurate at the time you prepared it? A. To the best of my knowledge, it was.

Q. And what is the date listed next to Marlin Investment Company? A. January 30, 1973.

* * *

[593] Q. I believe on cross-examination you characterized this as an on-paper note, is that correct? A. Correct.

Q. What did you mean by that? A. That is the form that is utilized by the bank. That was the jargon that was utilized. It is a yellow form normally associated with an unsecured loan, [594] although this particular loan was not. The reason that that note was utilized rather than a secured note form was because we believed the primary source of repayment was going to come from the operations of the coal mine and the gas fields and the collateral that was taken at that time was in what we call side collateral or lien collateral, and that was basically under a security agreement which was given to us in connection with the loans.

Q. Now, the loan itself, the first loan, Government Exhibit 1 is dated October 20, is that correct? A. Correct.

Q. And it was effective that day? A. Yes, it was.

Q. But it was granted on the 19th? A. All the paper work was filled out and we committed on the 19th to the loan.

Q. You had a meeting of the minutes on the 19th? A. That's right.

Q. But no moneys flowed out until the 20th? A. That's correct.

Q. And that was the same day you received the American Leisure stock? A. Yes, I believe that is the same day that we received the American Leisure stock.

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[598] A. My understanding of the functions were that Rubin was the financial man. He answered questions on financial matters and spoke to the bank about financial information. Deaton was the operating man. Whenever you would get into specifices on coal or natural gas, that is when he would speak.

That is what my impressions were.

Q. How did you reach those impressions? A. From conversations with both gentlemen.

Q. Do I take it your conversations with Mr. Deaton were directed in the same or different areas from your conversations with Mr. Rubin? A. Most of the time different. If they were there together then Rubin would answer the financial questions and Deaton would answer the operating questions as far as coal and gas.

Q. You testified in cross-examination that Mr. Rubin appeared to have some relationship to financial affairs of the company, is that correct? A. That is correct.

Q. Upon what did you base that conclusion? A. From conversations with him on financial matters. He was the one that I spoke to whenever there [599] was anything of finance that had to do with Tri-State Energy.

Q. Did he appear to be knowledgeable about it? A. Yes.

Q. Do you recall being asked on cross-examination about prior dealings of the bank with Englander & Bernstein, the accountants? A. Yes.

John Joseph Keating—for Government—Redirect

Q. Do you know whether the bank had any prior dealings with Mr. Rubin? A. Yes.

Q. And did that affect the making of the loan in any way? A. Yes, it did.

Q. How was that? A. Well, he was known to Ray Ludwig, who was the office manager, the chief lending officer of the office, and he was, to my understanding, respected as a knowledgeable accountant.

Q. Did the bank's knowledge of Mr. Rubin affect, in any way, the kind of background checking done on the borrower? A. Yes. We normally, if an account was being [600] brought in by someone that was well-respected, well-known to the bank, you would not normally do the amount of background checking that you would if somebody walked in off the street or was introduced to you from someone that you didn't know at all.

Q. Now, did the fact that Mr. Rubin was known make it harder or easier for Tri-State to get a loan? A. Easier.

Q. Have you personally ever dealt with Deaton or James previous to Tri-State Energy? A. No, I had not.

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[605] Q. I believe on cross examination you were asked if as of February 26, 1973 any of the notes were in default, do you recall that? A. Yes.

Q. And you answered that they certainly had matured? A. True.

Q. Is there a difference between the two? A. Default has the connotation that the loan is more of a loan agreement where you might set down certain specifics that a company would have to live up to and if it didn't live up to it then you would have the right to accelerate the loan before its maturity. These loans had matured but we still

—they were due and payable, but we didn't consider them at that time to be in default. We still thought we would get paid.

Q. Is there a reason you didn't consider a default? A. Because we felt we would be paid.

Q. What was the basis for that thought on your part? A. Discussions with the officers of Tri-State Energy.

Q. Was there anything that compelled or obliged the bank to make the new loan or the new note evidenced by [606] the February 26th demand note? A. Nothing.

Q. That was discretionary? A. Yes, it was.

Q. Could you at that point have simply let all the notes mature? A. Yes, we could.

Q. And at maturity, could you have demanded payment? A. Yes, or before, if we so chose.

Q. If there was an event permitting it? A. Yes.

Q. Why again did you choose not to follow that course? A. The normal policy of the bank when there was a work-out loan or a problem loan was to put it on a demand basis in one note.

Q. If there was no hope of repayment at the time, as maturity approached, what would you have done? A. I don't know. I most likely, I can only say that I probably would have let the loans mature and sent it to the Legal Department for collection.

Q. And sold the collateral? A. Yes.

Q. The October 20, 1972 financials, you made loans [607] to Tri-State after you got those financials? A. Yes.

Q. And were you aware of the contents of those financials when you made those later loans? A. Yes.

Q. And the first collateral you received was October 20th, correct? A. That is correct.

Q. And you received other collateral later, is that correct? A. That is correct.

John Joseph Keating—for Government—Redirect

Q. And did you make or continue to make loans after you received subsequent collateral? A. Yes, we did.

* * *

[608] Q. That projection, Document A9, had you received it before or after the December 6, 1972 loan for $275 thousand while it was made? A. I believe before.

Q. Did you take it into account with respect to that December 6th loan? A. Yes.

Q. What about the November 30th $100 thousand loan? A. I believe that I had the projection at that time and that it would have been taken into account also.

Q. And that projection, if you turn to it, A9, the top line, does it refer to the length of the projection? A. Yes, it indicates that it is a three-month projection.

[618] Q. Mr. Keating, the length of maturity of these notes to which you have testified, the three-month notes you had, and when I say you, I mean the bank, had the authority, did you not, in the event that checks were bouncing to call a note? A. Yes.

Q. So that actually the maturity of the notes which had been issued up to December 6, 1972 totaling $475 thousand, could have been called by virtue of the events [619] which occurred at the bank to which you made reference of alarming overdrafts by Tri-State Energy? A. Yes, they could have been called prior to maturity.

Q. But they weren't? A. They were not.

* * *

Thomas Cox—for Government—Direct

[649] THOMAS COX, called as a witness by the Government, being first duly sworn, testified as follows:

Direct Examination

* * *

[680] Q. You mentioned earlier some stock. Did Mr. Rubin tell you how Tri-State got the Allstate stock? A. Allstate Life Insurance stock I think was obtained from a Herbert Berg. I'm not sure just who, whether Deaton knew Herbert Berg. But—

> Mr. Bender: Again, excuse me, your Honor, is this his own recollection or is he talking about what Mr. Rubin said?
>
> [681] The Witness: This is my recollection of what Mr. Rubin told me or told us.

A. Rubin, when he was with North American Planning Company had Bank Computer Stock and I believe the Bank Computer had a value to it and all the other stock that Mr. Rubin described was shell corporations, meaning that they were legally incorporated, these corporations were legally set up, but they did not have any, any assets. They had no value. They did not have a business. They did not have any office and all they were were names with the legal authorization to issue stock.

Q. Again, this is as Mr. Rubin told it to you? A. Now, that is my understanding, and this is it, maybe not his words, but these, these are what these corporations consisted of. These were shell—his words were "shell corporations".

Q. Okay. Only tell us what Mr. Rubin told you. A. It's pretty hard to remember the exact words.

The Court: Your best recollection. She is not asking you for the exact words. Give us your best recollection of what he said.

A. My best recollection was that these were shell corporations without assets. He didn't say without—he said, "*shell corporations.*"

[682] And that they rented these stocks and buy—

Q. Who are "they"? A. Tri-State Energy, Deaton, James. Whether that includes Rubin or not, I don't know. Mainly Deaton and James. They rented it. They paid money for the use of the stock and the purpose for renting the stock was to use it as collateral for bank loans, and in addition to Deaton and James there was another individual, an Owen Oons, who is going throughout the country, Albuquerque, Florida, and he was pledging this stock or he was using this stock as collateral to get back loans.

Q. Which stock? A. Allstate Life Insurance. I'm not sure about Bank Computer. I would have to look up the names. There were several stocks. Allstate Life Insurance was one. I'm not sure if they used Charter Financial. They had two and a half million shares of Charter Financial.

Q. As to Allstate, did he tell you how that particular stock was obtained? A. Which one?

Q. Allstate. A. Allstate Life Insurance was rented from a Herbert Berg.

Q. Whose word was "rented"? [683] A. Rubin's word.

Q. Continue. A. As I say, I don't recall who contacted Herbert Berg or how Herbert Berg was contacted.

Q. Did he tell you anything about the transaction that you do recall? A. To explain it I have recollections of Allstate Life Insurance and the other stocks that came in

and I have recollection from other individuals that told me about it.

Q. Don't tell us about that. A. Yes, but I'm trying to separate what Rubin told me from what I know about it, and I would say other than him mentioning Allstate Life Insurance Company and him knowing that it is—it was without value and that it was going to be used as collateral, I don't think I recall just exactly what it was.

Q. Did he tell you when he knew that it was rental? A. He knew that these were valueless all along, that they were rented stocks, yes.

Q. What do you mean by "all along"? A. Whenever the Tri-State acquired it he knew. In May I think he first became associated with these individuals from Tri-State in the early part of 1972 in [684] May, and they incorporated Tri-State Energy something like June 12 of 1972, and all these series of what they did is on paper they would transfer millions of tons of coal in-ground and they would purchase this stock on-paper secured by reserves in the ground, and they would pay the individual that had it, they would pay him in cash a certain amount of money.

Q. Again he called this what? A. These were rented stocks.

Q. Did he tell you anything about Satellite Systems and Marlin Corporation stock? A. They were obtained from a Medwin Benjamin. Medwin Benjamin, a Peter Crosby and a William Hamilton. Somebody contacted James, either William Hamilton or Peter Crosby, and said that he could, the Medwin Benjamin—Peter Crosby did. Peter Crosby called James. And Peter Crosby told him that he had stock that he could rent, that he could use as collateral in the bank. And those stocks were Satellite

Systems and the other one you just mentioned. Peter Crosby at the time was a fugitive. And he—

> Mr. Bender: I am going to object to that, your Honor. Is this another thing—
>
> The Court: Is this something that Mr. Rubin [685] told you?
>
> The Witness: Mr. Rubin told me that.
>
> Mr. Bender: I object to it anyway, is that something that Mr. Rubin is saying that he learned in 1974, '75, '76, or whenever this man is testifying that he interviewed Mr. Rubin? Is this an impression we are trying to create that this man knew that it was with Tri-State in 1972? I object to it. I think it is improper.
>
> Ms. Neugarten: May we ask when the witness knew—
>
> The Court: When did Rubin say that he knew that Mr. Crosby was a fugitive with relation to the activity at the bank?
>
> The Witness: At the particular interview we had with Mr. Rubin, Rubin knew at that interview that Crosby had been a fugitive, and he knew at the time that William Hamilton brought up the stock or brought the stock to Tri-State Energy that Peter Crosby was a fugitive.

Q. He knew it at the time that Mr. Hamilton brought the stock, is that what you are saying? A. The reason I have to think so much is because a lot of people have told us what happened, and Mr. Rubin told us what happened, but at the time that William Hamilton brought the stock Rubin knew that he [686] was a fugitive.

Q. That is what Mr. Rubin told you? A. That is what Mr. Rubin told me.

Q. Again we only want to hear what Mr. Rubin told you, okay? A. I'm trying to separate what Mr. Rubin told me from what other people have told me.

Q. Did Mr. Rubin tell you what the terms were for Marlin and Satellite? A. I don't think he did.

The Court: When you say the terms were, what do you mean?

Ms. Neugarten: I don't want to lead the witness your Honor.

A. What I understand you mean by the terms is what they had to give to get the stock, how much money they had to give or what they had to give in return for it. Is that it? I don't think he know or he didn't mention what they gave.

Q. Going back to Allstate, did the witness tell you anything about a Jerry Marshall? A. Yes, he did.

Q. Can you tell us what that—I said did the witness tell you, I'm sorry. Did Mr. Rubin tell you anything [687] concerning Jerry Marshall? A. Jerry Marshall was a stock broker that Rubin knew personally. And they had pledged this stock at, or they were going to pledge this stock at Bankers Trust Company and they wanted to give a value to it, Deaton wanted to give a value to it. So Deaton wanted a price in the pink sheets. The pink sheets are the national—the over-the-counter market. I think the National Quotation Service. They print the sheet. They print the price each day of the transactions. And these prices come out on sheets that are colored pink and they call them pink sheets.

So Rubin introduced Deaton to Jerry Marshall. Deaton told Rubin to buy a hundred shares of stock and he gave a check made out to cash for $2200 for the stock.

Rubin endorsed this check and he gave it to Jerry Marshall, and the reason that Deaton didn't want—let me see —no. He asked Rubin to make out his own check because he didn't want Tri-State Energy connected to the sale. He wanted this a transaction that was done by somebody that was not related to Tri-State or that they couldn't identify —that anyone could not identify as to who bought the stock, so Rubin made out his own check for $2200.

[688] And he gave it to Jerry Marshall with the instructions to buy 100 shares of stock. I believe the price was $20, and that this price appeared in the pink sheets. Rubin never received any stock for this transaction. Rubin knew the trader, the Jerry Marshall brokerage company was a man named Al Reeves, and Al Reeves said he never placed an order for the stock because this stock was not available, there was no place to buy it for one thing.

Q. This is what Mr. Rubin told you? A. That's right.

* * *

[717] Q. Do you recall what stock it was with with which Mr. Lipsitz was mentioned by Mr. Rubin? A. American Leisure.

Q. Do you recall what it was that Mr. Rubin said about American Leisure?

* * *

A. Yes, I do.

Q. Could you tell us what it is? A. Rubin said a lot of things about American Leisure and one of the things he said was that 400,000 shares of American Leisure stock were brought in to Tri-State Energy through Jack Lip-

sitz and Ira Blue. Lipsitz was apparently the owner of it, and Ira Blue was the attorney. This stock was used as collateral at the Bankers Trust Company to secure bank loans for Tri-State Energy.

[718] Q. Did Mr. Rubin tell you what the price of that stock had been, if you recall? A. I don't recall the price of the stock.

Q. Did Mr. Rubin tell you how the stock was acquired, if you recall? A. I just recall the general way in which all the stock was brought in which was that these were all shell corporations and they were brought in and they didn't have any real—

> Mr. Bender: I move to strike the answer as unresponsive, your Honor.
>
> The Court: In other words, you don't remember anything specific Mr. Rubin said, is that it?
>
> The Witness: I remember 400,000 shares of American Leisure were brought in to Tri-State Energy. I remember that American Leisure was placed—
>
> The Court: Is this something Mr. Rubin told you?
>
> The Witness: Yes. This stock was pledged in the bank on collateral for the loans that Tri-State Energy was requiring.

* * *

[723] Q. Did Mr. Rubin tell you anything regarding an advertisement at Satellite Systems? A. Medwin Benjamin, I believe that's his name, placed advertisements in the International Herald Tribune and in that advertisement he would list a series of stock and one of the stocks that was listed, was Satellite Systems, and I believe he

established the price at the last sale as $20 for that stock and they took that advertisement—when I say "they," either Deaton, James or Rubin, they took that up to Bankers Trust Company and they established the value of Satellite Systems that was pledged with Bankers Trust Company, as collateral, a value of $20 a share for that stock.

[724] Q. And did Mr. Rubin tell you anything regarding his opinion of that value? A. Well, all along we discussed this or he discussed it that these were all shell corporations with stocks that had no inherent value—

> Mr. Bender: I move to strike the answer as unresponsive.
>
> The Court: Can you remember what he told you or are you telling us the substance of what he told you or what?
>
> The Witness: Well, in these conversations that we had, there were 12 conversations or more, he explained the way Tri-State Energy operated, the way they took the stock and they went up and secured the bank loan with the value of the stock, and then he explained where the stocks came from, what the stocks were and how values were placed upon the stocks, how they established the value so the bank could place a value on it, and show that the collateral was equal to the bank loan or greater than the bank loan.

Q. Did he tell you anything regarding his opinion of th se values? A. This thing on the International Herald-Tribune or the value of the stocks in general or what? He [725] established the value of the stock through his own efforts. There was a stock, I believe Allstate Life

Insurance Company, and Deaton wanted to get a price for the stock.

> Mr. Bender: I object to this. I think we are on Satellite Systems. I don't know how we got into Allstate. I don't think there is any question about Allstate at this moment, is there?

Q. Do you recall anything on Satellite Systems? A. Only that it had a price of $20 in the International Herald-Tribune advertisement, no; and that it was pledged as collateral for a bank loan for Tri-State Energy.

Q. Do you recall if Mr. Rubin told you how much Tri-State had paid for Satellite Systems? A. Yes. Satellite Systems and Marlin Investments were obtained from Medwin Benjamin, and they were the stocks that were obtained through Peter Crosby who used William Hamilton as an intermediary to deliver the stock.

> The Court: Which stock is this again?
>
> The Witness: Satellite Systems and Marlin Investments. Crosby had a conversation with James to say that he—that Medwin Benjamin had the stocks and Benjamin was willing to let these stocks be used as collateral for loans. Benjamin wanted, I believe, 7 [726] per cent—he wanted a 7 per cent rental for the stock and if it was not returned he wanted one-half the bid price of the stock on a certain day. So Hamilton delivered the stock to Tri-State Energy or he wanted the stock returned.
>
> Benjamin wanted the stock returned if he didn't get those figures. I forget, 7 per cent of the value

—anyway, Benjamin never received any money for the stock and he got very upset and he kept calling up and he wanted money for his stock.

Eventually Benjamin sent an individual up to Tri-State Energy to enforce the demand for money for the stock and Deaton in turn called upon somebody else to tell this man that came up—I forget how it was worded but anyway, to tell him not to try to get money for the stock.

Q. Did Mr. Rubin tell you who prevailed? A. Deaton's man prevailed.

Q. Did Mr. Rubin mention anything to you about projections? A. Yes, Rubin made the projections for the company. He would project how much the company would sell in a given period of time, how much revenue they could anticipate and so forth.

[727] Q. Did Mr. Rubin tell you anything about an Owen Oons? A. Yes, he did.

Q. Do you recall what that was? A. Owens Oons was an attorney who was going through the United States trying to get loans for Tri-State Energy and pledging the stock that we have been talking about as collateral for the loans.

Q. Did he indicate whether Mr Oons succeeded in getting loans? A. Owen Oons succeeded, according to Rubin, in getting somewhere between, I believe, $350,000 and $500,000 in loans for Tri-State Energy.

Q. Did Mr. Rubin tell you from banks in what part of the country those loans were obtained? A. One was the Bank of Alburquerque, and he mentioned banks in Florida and I believe another state.

Q. Did Mr. Rubin tell you anything regarding stock of a company called Management Dynamics, that you recall? A. He mentioned Management Dynamics, yes.

Q. Do you recall what he said? A. That was another stock that they brought in to Tri-State Energy and I forget the terms, and I forget how he brought it in.

> [728] Mr. Bender: How he brought the conversation in or how he brought the stock in?
>
> The Witness: The term is Rubin's, he brought it into Tri-State Energy, it's not mine.

Q. Is there anything that would refresh your recollection about Management Dynamics? A. That also would be in the notes here.

Q. Would you please take a moment to look at them. That is Government Exhibit 66 for identification, which are the notes you are referring to, Mr. Cox? A. The notes I am referring to are 66 for identification, yes.

[729] I see a reference here to Management Dynamics, and I think it refreshes my memory of what happened with Management Dynamics.

* * *

All right, your recollection is refreshed. You can look for the date later. A. Right, yes, I do.

Q. And do you recall what it was? A. Rubin said that James brought negotiated Management Dynamics and that is what the note said. I recall, and it should be here in the rest of it, that Tri-State Energy bought a certain amount of shares of Management Dynamics for $140,000. They took Management Dynamics and they pledged it at Bankers Trust Company.

Thomas Cox—for Government—Direct

Then the company itself, Management Dynamics, could not account for 900,000 shares so the SEC, the Securities and Exchange Commission, said to stop trading in the stock.

Then since the stock became restricted, it [730] was not good collateral at the bank. So Tri-State, either Rubin or James, went to the president of Management Dynamics and,—I jumped a little ahead of myself. This was gotten through two people, Freddie Remick, and some guy named Gottlieb, and they had a brokerage commission of $40,000, and the value of the stock was $100,000. So the president of Management Dynamics agreed to give them back $100,000, but they couldn't get the other $40,000 because he had never received it and this was a brokerage commission.

So then Rubin went back to Bankers Trust Company and went back and saw Keating and told Keating he wanted Management Dymanics returned to him and he would substitute another stock for it.

Q. Did Mr. Rubin tell you the reason he gave Mr. Keating for wanting it returned? A. The reason he—that he told Keating?

Q. Yes. A. He wanted the stock back?

Q. Yes. A. No, he didn't explain that the trading in the stock was stopped and I forget the reason he gave Keating, but the reason he gave us for doing this was in order to keep the Bankers Trust Company loan in good [731] standing, that it was not secured by collateral that was not acceptable to the bank.

Q. I'm not sure I understand your last answer.

Is it your testimony that he told Mr. Keating that the stock was not traded or he told Mr. Keating anything else? A. He told Mr. Keating something else. He did not give Keating the real reason why he wanted the stock back.

Mr. Bender: I object to that and move to strike it out unless we can get really what the conversation was. It's a conclusion on his part.

The Court: Is this something Mr. Rubin told you?

The Witness: This is something that Rubin told me.

Mr. Bender: You mean those were the words that he told him that he didn't give Mr. Keating the real reason or—

The Court: Is that it?

The Witness: The word "real" may not be appropriate there. He did not give Keating the reason that Rubin had for taking the stock back.

* * *

[819] Q. If you go back to page 7, isn't it a fact that just preceding that there are notes which indicate that he was asked about Satellite, he was asked about Marlin, he was asked about Hamilton, Peter Crosby; isn't that correct?

Isn't that correct, sir? A. No, I—I don't read it that way.

Q. What's your recollection? A. My recollection is that they pledged Marlin Investment at Bankers Trust Company and then after they pledged it, the company Marlin found there were 900,000 shares of stock unaccounted for and they asked the SEC to prohibit trading in the stock which meant that the stock then [820] pledged at Bankers Trust was no longer good collateral for the loan. So then Rubin went up to Bankers Trust Company, got the stock back from Keating and substituted another stock for that.

Q. Mr. Cox, isn't it a fact that Mr. Rubin told you guys that in his opinion at the time you interviewed him these certificates of stock were "shit"? A. That's right.

> Mr. Bender: Forgive me, your Honor, but that's a quote. I mean, it is right in the notes, so I apologize to anybody who is offended by it.

Q. Isn't that the way it appears in the notes? A. Does that mean it's restricted?

Q. No, but the word I used, which I am blushing at, isn't that what the note says? A. Yes.

• • •

[926] MAX ENGLANDER, called as a witness on behalf of the government, having first been duly sworn, testified as follows:

(Direct Examination)

• • •

[939] A. The next document is Exhibit 122 which is the pink sheet referring to the bank computer network stock value which was circled and this was referred to in my report, in the text of my report under "Investments, Part 2B."

Q. Which exhibit are you referring to? A. Exhibits 96 and 97.

Q. What date is the pink sheet? A. It looks like July 12, 1972.

Q. And Exhibit 123? A. 123 refers to All States Life Insurance Company which is the pink sheet which gives me what you can buy the stock for and what you can sell the stock for.

Q. Can you tell its date? A. It looks like July 12, 1972.

Q. Would you describe for us how you went about the preparation of the July 11th balance sheet and the report dated as of July 18, 1972, which accompanied it? A. Well, the text is July 18th and the reason the text was not written until July 18th is because I was waiting for the letter from the Chelsea National Bank. That letter was dated July 18th and that confirmed the amount of cash that was reflected on the balance sheet. The other items I had received on July 11th since my report was as of that date, I used the pink sheets for the purpose of [940] commenting what those stocks were worth as of that day but on the balance sheet they were reflected at cost only.

All the other items that we were going under the exhibits were in preparation of that July 11th report.

Q. Each of those items was supplied with the exception of the letter from Chelsea Bank, it was supplied by Mr. Deaton? A. Yes.

Q. And the Chelsea Bank letter? A. Was signed by a Larry L. Bornstein, Senior Vice President.

Q. And was sent directly to you? A. Yes, ma'am.

• • •

[1119] CHARLES LEEDS, called as a witness by the Government, being first duly sworn, testified as follows:

(Direct Examination)

• • •

[1120] Q. As associate general counsel of Bankers Trust in 1973, did there come a time that you attended a meeting

in May 1973, at which time Mr. C. W. Deaton was present? A. Yes.

Q. Do you recall who else was present at that meeting? A. Mr. Gene Brinker, who is a first vice-president of the bank, William Powderly, who worked with Mr. Brinker, Steven Fried, who worked in the bank's 39th Street and Broadway office, myself, Mr. Deaton, and that is it.

Q. Were you present from the outset of the meeting? A. I may have arrived seconds after the commencement of the meeting.

[1121] Q. Do you recall who did most of the talking at that meeting? A. Mr. Deaton. * * *

* * *

[1127] Q. What was the occasion for this meeting? A. Mr. Deaton was explaining that there was no possibility of recovering any money from Tir-State Energy Corporation, which was indebted to the bank for a specific sum of money at that time, by reason of the fact that Tri-State did not have any assets or any collectible assets, but that a corporation in which Tri-State had an interest, General Oil & Gas, did have some possible assets and if these assets were exploited, there would be a possibility of [1128] recovering a certain amount of money to satisfy or partially satisfy the Tri-State indebtedness to the bank.

But for this purpose Mr. Deaton had indicated that he would require an additional sum of money and we all assumed that that was the purpose of the meeting, to get additional loans from the bank for assumedly these purposes.

* * *

Q. The money, the additional monies that were being requested for Mr. Deaton personally or for some other

business? A. It wasn't made entirely clear but I was under the impression that he wanted to borrow these monies through the corporate vehicle, Tri-State.

Q. As had been done before? A. Yes. He was already a guarantor for Tri-State so he was also looked upon as personal vehicle of collection by the bank.

Q. Do you recall if there was any discussion of leases at that meeting? A. I can't say specifically. It is just that at one particular time I interrupted Mr. Deaton and I asked him whether the leases with regard to the assets he was talking [1129] about, and I wasn't certain at that moment just what assets he had in mind, were still available or whether or not they had expired.

He had indicated that they did expire, but he didn't think there would be any problem in getting them reinstated or reviving the leases.

Q. And what again was the date of this meeting? A. The date was May 14, 1973.

Q. As a result of the meeting, did the bank extend further loans to Tri-State Energy? A. No.

Q. Did you, as of that time, commence a lawsuit against Tri-State Energy? A. Shortly thereafter.

Q. Approximately how much money in total did the bank recover as to the total loans it had extended to Tri-State Energy?

> Mr. Bender: I object to that as far as it being beyond the period that we mentioned and not binding upon Mr. Rubin.
>
> The Court: Overruled.

A. $2,500.

Q. $2,500? A. Yes.

[1130] Q. And the loans were 475 thousand? A. Yes.

* * *

John E. Pinto, Jr.—for Government—Direct

[1203] JOHN E. PINTO, JR., called as a witness by the Government, being first duly sworn, testified as follows:

* * *

Direct Examination

* * *

[1211] Q. Directing your attention to July, that is advancing a month from June 1st, did you ever have any conversations regarding the financial problems and possible solutions at North American Planning? A. Yes, I did.

Q. With whom did you have such conversations? A. With both Mr. Goldenberg and Mr. Rubin.

Q. Can you recall if any proposals were advanced by North American to solve its problems in July? A. Yes, in July we received a financial statement from North American Planning for the month end June 30, 1972, and on that financial statement we noted that there was an increase in the firm's capital of approximately $190,000 and upon review of the financial statement we found that the reason for that increase was that the firm had subordinated 10,000 shares of All States Insurance Company of Alabama. We, at that point, had some questions about the All States Insurance Company of Alabama from a liquidity point of view and thereafter had conversations both with Mr. Rubin, Mr. Goldenberg regarding that.

Q. Would you relate to us the substance of those conversations regarding All States? A. May I refer to my notes on this? [1212] A. Yes, if you refer to any notes would you indicate their number. I believe you will find a four digit number in the corner of each. A. Okay. This is 3615AAA.

Q. If you, rather than reading from the notes, can refer to them to refresh your recollection and then testify. A. Okay. On July 14 I spoke to Mr. Goldenberg regarding the firm's net capital for the period ending June 30. If the 10,000 shares of All States Insurance were given full value the firm would have been in compliance with the net capital rule. One of the things that you have to consider when reviewing for net capital is the liquidity of the assets.

The net capital basically is a liquidity rule, how rapidly and how quickly can these assets be converted to cash.

In reviewing the 10,000 shares of All States I reviewed the pink sheets to determine whether there were any marketmakers in the security and upon reviewing I found that there were two marketmakers in the pink sheets and as was our standard procedure at that time for large blocks of stock in a limited number of marketmakers we surveyed the two marketmakers to determine how liquid this position was.

[1213] In other words, they as marketmakers and as a marketmaker, I mean this is a broker dealer who stands ready to buy and sell a security and he publishes his quotations in what is called the pink sheets, at least at this time we are talking about the pink sheets.

Basically the pink sheets are really an interdealer quotation system. It is a place broker dealers go to publish what their quotes are to say I am willing to buy and sell at these prices.

So we looked at the pink sheets and found that the two broker dealers that were in the sheets were only in on the bid side and the bid side means they were only looking to buy shares.

They were not on both sides of the market.

John E. Pinto, Jr.—for Government—Direct

We found that through conducting the survey of the two marketmakers that there was very, very little trading activity in the security and, as a matter of fact, we made a determination that of the 10,000 shares of All States only 200 shares could be considered as an allowable asset for net capital purposes.

That was brought about by the fact that between the two marketmakers who had been in the sheets for six weeks or so they had only done 100 shares between them.

[1214] Q. Continue with your discussions.

* * *

A. I advised Mr. Goldenberg that based on our determinations as to the liquidity of the 10,000 shares of All States that we would not be able to give them a liquid asset value for it and based on that determination the firm was not in compliance with the SEC's net capital rule for the end of June.

The ramifications of that could have been that we would have requested that the firm cease doing business [1215] in securities.

Mr. Goldenberg rseponded by stating that he had two alternatives at this point, one of which was to sell the 10,000 shares of All State back to the issuer and convert that cash into assets for the firm or as an alternative take the 10,000 shares of All States, pledge them as collateral for loan at a bank and then put that money which is received by collateralizing the loan into the firm as capital, thereby increasing the firm's net capital.

These were the two positions. He also raised the question or the possibility of North American Planning's involvement with 2.5 million tons of coal. He expected some half million dollars in some sort of commissions as a result of a sale of that coal and he said that that half mil-

lion would also be coming into the firm and would increase the firm's net capital.

* * *

[1219] Q. Did you discuss the All States at any other time? A. On July 19th I spoke to Mr. Goldenberg. I was calling to find out the relationship between Tri-State and All States. I was advised at that point that Tri-State had invested $1 million in All States Insurance and in return for that Mr. Goldenberg believed the firm had received stock and part ownership in all States Insurance.

So that according to Mr. Goldenberg, there was a definite relationship between Tri-State and All States Insurance. The reason why I was asking the question is based on my discussion with one of the market makers, I determined that there were only 120 thousand shares of All States Insurance outstanding in total. Of that 120 thousand, there were only about 1,300 that were publicly traded in the hands of the investors.

My question came as to the marketability, not from the point of view of liquidity at this point, but were these restricted shares, was there any legend on these shares that would prohibit the seller or the owners of the shares from going into the marketplace and selling them.

So my purpose in asking the question, one of the factors in determining whether it is restricted stock, would be the relationship between the owner of the shares and the [1220] issuer itself.

In this case, based on my discussions, there appeared to have been a relationship between Tri-State and All States Insurance.

I think that basically covers the All States.

Q. Did you discuss that possible restriction with anybody else? A. I discussed the restriction in the trading

of the shares with Mr. Goldenberg. I am just looking for the date. I discussed them with Mr. Goldenberg and subsequently had a conversation with Mr. Rubin. On July 19th I had this conversation with Mr. Goldenberg. Right after that I talked to Mr. Rubin and although my memorandum does not specifically say that I reiterated everything that I had just discussed with Mr. Goldenberg, my recollection of the fact is that I would have reviewed what I had just discussed with Mr. Goldenberg because of the relevance and importance of whether or not these shares were restricted shares.

Q. I believe you said that your question was occasioned by the fact that there might be only 12 or 13 hundred shares in the hands of the public, is that correct? A. Yes, ma'am.

Q. Did you understand that that in some way might effect marketability? Was that your understanding at the [1221] time? A. Yes, that would definitely have meant that there was a very, very thinly traded market for the shares. In other words, if there is only 12 or 13 hundred shares in the public's hands that is freely tradeable, that is the fullest extent of what can be traded without any kind of restrictions on the sale of the securities. So that would have severely impacted the ability to sell those shares.

Q. Handing you what has been marked as Government's Exhibit 87 for identification, a photocopy of a document. A. This is a copy of the subordination loan agreement which was filed by North American Planning with the SEC with a copy to the NASD dated June 30, 1972 wherein Tri-State Energy was subordinating the 10,000 shares of the common stock of All States Insurance Company to which they attributed a value of $190 thousand.

Q. By whom does that appear to be signed? A. The lender is C. Deaton—I can't read the middle initial, and the borrower for North American Planning is signed by Eugene Goldenberg.

Ms. Neugarten: At this time the government offers Government's Exhibit 87 for identification into evidence as Government's Exhibit 87.

Mr. Bender: Is this also on background, your [1222] Honor, or is this for the truth of the contents of this agreement? If it is, I object. If it is just for background, then I don't see any reason for it. I don't know what it is put in for.

Ms. Neugarten: The government has urged throughout the trial and the indictment urges that All States stock was later pledged as collateral at Bankers Trust by Tri-State, including at that point Mr. Rubin, and that the government's contention is that Mr. Rubin should have known from his conversations with Mr. Pinto something about All States.

This is the documentation which led to the conversation with Mr. Pinto. And it places a value, according to Mr. Deaton and Mr. Goldenberg, on the stock, of what they were telling to the NASD. That goes in as background of a conspiracy that starts at Tri-State weeks later, only a few weeks later.

* * *

[1230] Q. Now, is there a difference in marketability between restricted stock and unrestricted stock? A. Yes, most definitely. As I mentioned previously, restricted stock, there are many procedural steps, there are a whole

time period for which you must hold the stock or relationship questions, all of which must be resolved before somone can sell restricted shares.

The SEC has adopted a rule, it is Rule 144, which specifically addresses the sale of restricted securities. Freely tradeable securities are very simple. You go to the marketplace in which the stock trades and you sell it without any course of delays or encumbrances.

Restricted shares, that is not the case. It is a rather involved process to sell restricted shares, and in some cases they cannot be sold.

Q. Now, you mentioned pink sheets. A. Yes.

Q. Could you tell us what the pink sheets are as best you understand? A. Pink sheets are an interdealer quotation system, wherein broker-dealers, who are making markets, as I mentioned before, broker-dealers who are advertising their bid and asked prices, the prices at which they are representing they are willing to buy and sell, they put these quotations in [1231] this interdealer quotation system for purposes of generating buy and sell orders.

Q. And which is the bid and which is the asked? A. The bid is the price at which they are willing to buy, and the asked is the price at which they are willing to sell.

Q. And to whom are pink sheets available? A. They are available to all broker-dealers, I know. And I think you can subscribe to get pink sheets even if you are a member of the public, if I am not mistaken. I'm not certain about that.

* * *

John E. Pinto, Jr.—for Government—Redirect

[1255] *Redirect Examination*

* * *

Q. Do you recall being asked in cross-examination, Mr. Pinto, whether you had firmly concluded one way or another whether the All States stock was restricted? A. Yes, Ma'am.

Q. Now, what was it that led you to believe that it might be restricted? A. During my conversations with one of the marketmakers I determined that there were a total of 120,000 shares in total that were outstanding in this particular security of which only 1300 were in the public's hands. The fact that we were talking about 10,000 shares of All States when there were only 1300 out in the public hands, I did not come to the very difficult mathematical conclusion that there were not enough shares in the public hand to fill the 10,000 shares that were being subordinated to the firm.

I, therefore, immediately raised the inquiry [1256] that if only 1300 are in the public's hands, the other at least 8700 shares are not in the public hands and, therefore, raises a question as to whether they were freely tradable.

In addition to that, I subsequently determined that there was a relationship between All States Life and Tri-State. That would raise even a further question as to whether the shares were restricted because even if an individual purchases on the New York Stock Exchange a freely tradable security, but his relationship with the issuer is of a control nature, those shares may, in fact, become restricted by that relationship.

So both of those conclusions, the number of outstanding, the number of freely tradable versus the 10,000

that were being subordinated and also the question at least that was raised as to the relationship between the issuer, All States, and the lender, Tri-State.

* * *

[1266] ALFRED REEVES, called as a witness on behalf of the government, having first been duly sworn, testified as follows:

Direct Examination

* * *

[1269] Q. Now, did there come a time in October of 1972 when you had a conversation with Jerry Marshall about All States stock? A. Yes, there was.

Q. And do you recall the substance of that conversation? A. As he had done in the past when he selected a stock for the house to trade, he would tell me that he had a particular stock. In this particular case he said had a new case for the house to trade All States Life Insurance Company of Alabama.

He gave me a stack of papers which I will use to file a 211 application with the National Quotations Bureau in order to get the stock listed in the pink sheets.

Q. Now, did there come a time that the stock was in fact listed at your behest in the pink sheets? A. Yes, it was.

Q. And do you recall approximately when that was? A. Approximately late October, 1973. I'm sorry, 1972, I think '72.

Q. Now, do you recall whether—that was after your conversation with Mr. Marshall? A. I recall it to be no more than two weeks. Normal procedure, when you file an application with the [1270] National Quotations

Bureau, they do whatever analysis they would normally do to determine whether the stock qualified for the pink sheets, and if they did, then they immediately notify you that it does qualify, and you are then free to list that stock with your broker-dealer name in the pink sheets.

Q. Now, did Mr. Marshall tell you why he wanted the stock listed in the pink sheets? A. He said he had an order on the stock.

Q. Did he indicate the amount? A. 100 shares.

Q. And did you have any further conversation with him regarding that order? A. I assumed at the time that since he had an order to buy the stock that the correct way of putting the stock in the sheets would be to bid for the stock, but he told me he wanted to make a two-sided market in the stock, offering the bid—having a bid and an offer in the stock.

Q. Now, do you recall—strike that.

Do you recall how the stock appeared the first day it was listed in the pink sheets? A. The market was to be 20 bid, 22 offered.

Q. And do you recall whether you had any conversation at any point with Mr. Marshall regarding the way the [1271] stock was listed in the pink sheets? A. We talked about—actually I talked about—he told me what to do—I took issue with him—when you put a market in the stock, it generally indicates that you are willing to buy and sell at the prices which you are listing in the pink sheets, and I warned him of the fact that by giving an offer of 22, that should somebody call up, another broker would be the type of person that would call, and ask for a market, and I gave him 20/22, and once I gave that market, I am obligated to sell him 100 shares if he wishes to buy it, and should we

have to sell somebody 100 shares at 22, I warned him that if the stock was not readily available in the market, and since we were the only market makers to be in that stock, I didn't see, couldn't see, where we would be able to find 100 shares, and I warned him that he could suffer a loss because of it, and that the firm, since it was marginally capitalized, it could jeopardize the net capital of the firm and perhaps cause its suspension.

Q. And did he do anything in response to your advice? A. He just said, "Leave the market at 20/22. Let's see what happens."

Q. Was there ever a point at which the stock was listed without a price by you in the pink sheets? [1272] A. Yes. From time to time—let me tell you the procedure that is used to create each day's quotation.

They provide computer cards to each firm that had the firm's code already punched into it. You would then write the name of the stock and the market that you wished to have show in the pink sheets on that. You then sent it to the National Quotations Bureau on any given day, and that would be the quotation you would show for the next day in the pink sheets.

Initially, at the beginning, maybe the second, third or fourth day, I don't remember which, I didn't put a quote. I put the card in but I did not put a quote on it because I was still apprehensive about putting a two-sided market. In fact, I think it was the second day that we prepared the sheets, I didn't put a market in because I didn't think he fully realized the jeopardy he was putting himself in as a firm.

The following day when the quote did not appear, he brought it to my attention immediately, and insisted that a two-sided quote be made at all times.

After that, from time to time, just through its called order, that because of the business of a particular day, I would forget to put all the cards in so that not only All States would be missing but other would be missing [1273] there were days when just the stocks that we were very active in got filled out and sent in and the ones that were inactive weren't sent in, but there was no rhyme or reason why the stock was listed or not listed on those particular days after the first miss.

Q. Well, did Mr. Marshall continue to instruct you to list the stock? A. Right. Every time that I missed, he would always bring it to my attention.

Q. And tell you to put it in again? A. Right.

Q. Now, you said that you went in on both sides of the market. What do you mean by that? A. In the pink sheets—let me just start from the beginning and explain what the pink sheets are for.

There are stocks that are not listed on the New York Stock Exchange or the American Stock Exchange or any other exchange. Many of these companies are in effect listed in the pink sheets, and merely what it does is to tell all the brokers who subscribe to the sheets that you have an interest in a particular stock.

If the stock qualifies, the name of the stock appears alphabetically in the sheets, and all the brokers who are interested, either on the buy side, the sell side, or [1274] both, are listed underneath the name of the stock.

I forgot the point I was going to make.

Q. Okay.

Now, how can you go into the pink sheets, in what different ways may a broker enter? A. Okay.

The pink sheets can either appear on a blank, which would merely indicate, after your name there would be nothing, and that would just indicate that you had some

interest in the stock, but you weren't ready to disclose what the interest was.

[1275] Q. This is what you did in that early day? A. Right, on the second day I believe it was. Just that you had an interest.

The way most stocks are listed are with the two-sided market, a bid and an offer. The bid represents the price at which you would be willing to buy the stock and the offer, the price at which you would be willing to sell the stock.

This is really only an indication because what you put in for Monday appears on Tuesday, and it tells everybody on Tuesday what you would have done on Monday. But anyhow, it's an indication that you are willing to buy and sell at these prices.

There is another way in which you can appear, and that is if you wish to disclose that you have a bid, but you don't want to disclose exactly what the bid is, you can put a BW into the sheets, which means bid wanted. I am sorry, it's the reverse. If you want to buy, you would be looking for an offer, so it would be offer wanted.

So if you wanted to buy the stock you would put an OW by your name and that would indicate to all those looking in the pink sheets that would entertain an offer, if they wanted to tell to you, you would be wiling to buy. The other side would be if you wanted [1276] to sell you would be looking for a bid from somebody else. You would want them to bid you for the stock, so you would put a BW in which you would be indicating that you wanted a bid for the stock.

And those are the ways in which it can appear in the sheets.

Q. Now, can you go in one side rather than both sides? A. Yes. You could go in with an actual number on the

bid side or you can go in with an actual number on the offer side.

Q. Now, when you go in on both sides, is there any consequence or rule with respect to being in on both sides? A. Any consequences? No, there is none.

Q. Now, is it an indication of any willingness to do anything? A. Yes, it is an indication that you are willing to buy and sell even though not perhaps at that particular price, but that you would be normally willing in the course of your regular business to buy and sell the stock.

Q. Now, Mr. Marshall said he had what kind of order? A. He said he had a bid; someone who wanted to buy 100 shares.

[1277] Q. Did he say he had anyone who wanted to sell any shares? A. No.

Q. So, for what reason were you in on the sell side? A. He wanted to be on both sides.

Q. Now, to the best of your knowledge, was the subject of payment for the stock ever discussed? A. Yes. I told him that the fact that he was putting in any type of market into the pink sheets that since we were the only market makers in the stock at the time, that if he did have in fact somebody who wanted to buy the stock, that the possibility existed that when the time came to call the guy up and say, "We've go the stock, we're selling it to you," and he says, "Oh, no, I changed my mind, I don't want it," he would then be stuck with 100 shares of the stock.

I suggested that if he in fact had an order in the stock that he get payment from the customer.

Q. Now,—and these pink sheets, to whom are they available, to the best of your knowledge? A. Any broker—I think it is any broker. I don't know if outsiders can get

it or not. But basically, brokers who subscribe to the pink sheets have them available.

Q. Now, did whoever—were you ever in fact able to execute this order? [1278] A. No, I never had an order in the stock. I never had an execution; no buys and sells.

Q. And did you ever hear of a company called American Leisure? A. Yes, I have.

Q. And how did you hear of them? A. It was one of the house stocks.

Q. And do you recall what its trading volume was? A. No, I don't.

Q. And is there a difference between the marketability of a—strike that.

Are you familiar with the concept of restricted stock as well as unrestricted stock? A. Yes, I am.

Q. And is there a difference in the marketability of the two? A. Yes, there is.

Q. And can you tell us in general layman's terms what that is? A. Basically, restricted stock, if it can be sold at all, is sold in a private transaction, because restricted stock normally is not freely tradeable in the open market and therefore, from what I know of the rules of the Securities and Exchange Commission, certain tests normally have to be [1279] met in order to transfer this type of stock, and therefore, the salability—the unsalability would reflect a lower market price or a negotiated price of the stock in a private transaction.

* * *

Donald W. Jennings—for Government—Direct

[1357] DONALD W. JENNINGS, called as a witness by the Government, being first duly sworn, testified as follows:

Direct Examination

* * *

[1368] Q. Now, did Mr. Rubin tell you anything regarding a business relationship between Bankers Trust and Tri-State Energy? A. Yes, he did.

Q. And can you tell us as best you recall, what he told you? A. Mr. Rubin said that Tri-State Energy had a great need for money, financing. And Mr. Rubin said that he had had a business relationship with Bankers Trust Company, and that he suggested that to Mr. Deaton, Mr. James of Tri-State Energy, that they try to arrange a loan through Bankers Trust Company, and he agreed to introduce them to people at Bankers Trust Company for that purpose.

Mr. Rubin told us that he and Mr. Deaton, at Tri-State Energy, made a trip to Bankers Trust Company to visit a Mr. Graziano, I believe it is, who had arranged for Mr. Rubin previously.

Mr. Rubin said that Mr. Graziano informed him and Mr. Deaton that the type of loan they were seeking was not within his purview, and Mr. Rubin said that Mr. Graziano introduced he and Mr. Deaton to a Mr. Ludwig who handled corporate loans.

* * *

[1374] A. The first meeting, according to my notes, where Mr. Rubin mentioned All States Life Insurance was the meeting of January 9, 1975.

Q. Was it mentioned at subsequent points as well? A. Yes, it was.

Q. What did he tell you about All States Life Insurance? A. Well, Mr. Rubin said several things about All States Life Insurance stock. He said that it was pledged by Tri-State Energy with Bankers Trust Company. He said that All States Life Insurance originally came through Mr. Deaton.

We asked him how Mr. Deaton acquired the shares of All States Life Insurance and he said that he didn't know but he believed that it was a deal between Deaton and Mr. Berg of All States Life Insurance and he believes that Mr. Deaton paid Mr. Berg in some way.

Q. Who believed— A. Mr. Rubin believed that Mr. Deaton had paid Mr. Berg for the issuance of All States Life Insurance shares.

Q. When you say paid, did Mr. Rubin indicate what he [1375] meant by that? A. Mr. Rubin didn't say that he knew that Mr. Deaton paid Mr. Berg, he said it was his feeling that Mr. Deaton had paid Mr. Berg for the issuance of the shares.

Q. Do you mean paid in what fashion, to the company or what? A. To the best of my recollection, Mr. Rubin indicated that Mr. Deaton had paid money personally to Mr. Berg, not to All States Life Insurance Company.

Q. To ask the question Mr. Bender is putting, do you mean under the table? A. Mr. Rubin didn't say that he paid him under the table. He didn't describe the nature of the payment.

Q. But that it was a "personal" payment; correct? A. It was my feeling that Mr. Rubin was saying that it was a personal payment.

Q. From sitting there and listening to what Mr. Rubin said? A. Yes, from listening to what Mr. Rubin said.

Q. Did he say whether he, Mr. Rubin, ever met Mr. Berg? A. To the best of my recollection, Mr. Rubin said that Mr. Berg visited the offices of Tri-State Energy on at least one occasion and that he had met him at that time.

[1376] Q. Did Mr. Rubin discuss anything regarding negotiations? A. Yes, Mr. Rubin said that at one time he was negotiating with Mr. Berg for the acquisition of 10 thousand shares of All States Life Insurance on behalf of Tri-State Energy.

Q. He, Mr. Rubin, was negotiating with Mr. Berg? A. He was negotiating with Mr. Berg, yes.

Q. When you say "he," if you can clarify it, it will make it easier for us all.

Did Mr. Rubin say anything regarding a Jerry Marshall? A. Yes, he did.

Mr. Rubin—

> Mr. Bender: Can I interrupt to ask whether we're referring to February 4, 1975?
>
> Ms. Neugarten: As to All States he said the first reference was January 9th and it occurred, he thought, at every meeting.
>
> Mr. Bender: I thought he said February 14th and then it occurred at other meetings.

Q. Did I state it incorrectly? A. You're right.

> Mr. Bender: I'm wrong then.

[1377] Q. On January 9, 1975, do you recall whether the date on the note for that meeting reflects '74 or '75? A. The date reflected is 1974.

Q. And it is your recollection that the meeting in fact took place when? A. In 1975.

Q. I believe I had asked you about Jerry Marshall. A. Yes. Mr. Rubin said that he had met Mr. Marshall while he was associated—while Mr. Rubin was associated with North American Planning, and that Mr. Marshall on one occasion had come to the offices of Tri-State Energy and raised a question concerning the possibility of Tri-State Energy being able to help him with some financing.

Q. Did Mr. Rubin say what business Mr. Marshall was in? A. Mr. Rubin said that Mr. Marshall was a stockbroker.

Q. Please continue. A. Mr. Rubin said that he introduced Mr. Marshall to Mr. Deaton and that Mr. Deaton tried to arrange a lease buy-back arrangement with Mr. Marshall with some company in Chicago for financing purposes and he said that this deal did not go through.

He said that on another occasion Mr. Deaton came [1378] to Mr. Rubin and requested that he place an order for 100 shares of All States Life Insurance stock through the firm of Marshall, Murray & Co., which is Jerry Marshall's brokerage firm.

He said that he asked Mr. Deaton, "Why do you want me to do this; what can't you do it yourself?" And he said that Mr. Deaton told him that Tri-State Energy has a substantial interest in All States Life Insurance stock and it wouldn't look right for him to place the order.

Q. For him, Mr. Deaton? A. For Mr. Deaton to place the order. He said that Mr. Deaton gave him a check for $2,100.

[1379] Q. Who gave who the check? A. Mr. Deaton gave Mr. Rubin a check for $2100 and that he indicated on the check that it was for another amount, $3800 or 3800-some odd dollars partial payment for some other purpose.

And Mr. Rubin cashed this check and issued his personal check to Marshall, Murray & Company for $2100.

Mr. Rubin said that he asked Mr. Deaton why he wanted to purchase this 100 shares of All States stock and Mr. Deaton, according to Mr. Rubin, said to him that he wanted the price of All States stock, $21 a share, to appear in the National Quotation Bureau's pink sheets so that the bank or banks could refer to these pink sheets in determining the value or a value for All States stock.

During this conversation Mr. Rubin said that Mr. Deaton also said that he wanted this price to appear so that the banks would be able to place a value on it for his purposes and also for the purposes of Mr. Ooms, who was obtaining loans using All States Life Insurance as collateral around the country.

Q. For Tri-State? A. I don't believe he said why Mr. Ooms was obtaining the loans.

[1380] Q. In interviews that you attended did Mr. Rubin at any point discuss what kind of stock All States was? A. Yes, he did. On one occasion—

Mr. Bender: Can we have a date?

Q. If you recall the date tell us. A. I believe it was January 1975. I had a discussion with Mr. Rubin concerning All States Life Insurance stock.

Q. Can you relate to us what that was? A. I asked Mr. Rubin if he didn't think that the stock that was pledged as collateral with Bankers Trust Company should have had a legend placed on the face of the certificates, a restrictive legend. Mr. Rubin said to me at that time that he didn't know if it should have had a restrictive legend or not. At that point I pointed out to Mr. Rubin that he was a principal and a registered broker dealer

and it was a publicly-owned company, that he was a CPA, that he was an attorney, that he was a principal in another large firm, Tri-State Energy, and that he had substantial experience in buying and selling stocks and to me it should appear that he shoudl be aware that a legend should appear on that stock.

> Mr. Bender: I object to this unless Mr. Jennings is actually telling the Court and the jury and all [1381] of all that this is exactly or in substance what he told Mr. Rubin, not his own operation of his own mind.

Q. I quite agree, is that what you told Mr. Rubin? A. That is the substance of what I told Mr. Rubin.

Q. Did he respond? I don't mean to cut you off. A. At this point Mr. Rubin became visibly upset with my question and he mentioned the fact that he had two small children, a sick wife, he was having a tough time finding employment.

Other than that he didn't respond to my question as to whether or not there should have been a legend or if he thought there should have been a legend on the face of those certificates that were pledged as collateral.

> Mr. Bender: I move to strike that statement that he made to Mr. Rubin. We are not being given a conversation that he had where Mr. Rubin made statements and the whole purpose of this is to indicate that Mr. Rubin made statements which the Government is claiming are in issue. This man's statements are not certainly admissible any more than a statement by the prosecutor as to a question to ask the witness.
>
> The Court: I don't know what you have in [1382] mind specifically.

Mr. Bender: This statement he says he made. I made a statement, he says, to Mr. Rubin, that you were a principal and a broker dealer, that you were a CPA, you were an attorney, you were an experienced individual and you should have known something about All States stock. And what did Mr. Rubin say? He said nothing about whether he should have known or didn't. All he says that he was visibly sick or he was visibly annoyed, his wife was sick and that he was unemployed.

The Court: He is telling us what occurred, that is what Rubin said and what he said, is that right?

The Witness: Yes.

The Court: What is the objection?

Mr. Bender: The objection is that I think the jury should be advised that what this witness from his own mind concluded of what Mr. Rubin's knowledge should have been is not evidence. It is only what comes out of Mr. Rubin's own mouth.

The Court: We went over that before. That was your prior objection and he said that was in substance what he, the witness, told Mr. Rubin.

Let's proceed.

Q. Did Mr. Rubin at any point tell you how much or [1383] what quantity of All States stock Tri-State had? A. To the best of my recollection, Mr. Rubin said that Tri-State Enegry had between 35 and 45,000 shares of All States stock.

* * *

Q. Do you recall whether Mr. Rubin told you anything about a company called American Leisure Corporation? A. Yes, he did. Mr. Rubin said that during his associ-

ation with North American Planning Corporation he had occasion to meet a Mr. Jack Lipsitz, who at one time had been a wealthy person and who was a person that dealt in what he called junk stocks.

[1384] Q. That is what Mr. Rubin said? A. That is what Mr. Rubin said. Mr. Rubin said that he had been requested by Mr. Deaton to seek public companies on behalf of Tri-State Energy.

Q. That he, Mr. Rubin, had been requested? A. He, Mr. Rubin, had been requested by Mr. Deaton to seek publicly-owned companies on behalf of Tri-State Energy and that Mr. Jack Lipsitz controlled American Leisure, which was a publicly-owned shell and he said that he introduced Mr. Lipsitz to Mr. Deaton and that as a result of that introduction Tri-State Energy acquired certain shares of American Leisure and that Tri-State Energy exchanged certain of their coal rights with American Leisure Corporation.

He also said that subsequently Tri-State Energy pledged these shares of American Leisure with Bankers Trust Company as collateral for their loans.

Q. Did he at any point—I am sorry? A. He indicated or he said, to the best of my recollection, that these shares of American Leisure that were pledged at Bankers Trust Company were restricted for sale. They bore a restrictive legend, restricted from sale to the public, and that Mr. Rubin in conversations with Mr. Ludwig said to Mr. Ludwig that he would try to [1385] have this restrictive legend removed.

Q. Did he tell you anything about the assets of American Leisure? A. Yes, Mr. Rubin did. He said that American Leisure was a shell, a shell corporation. To

the best of my recollection, I believe he said that they had a claim or a lawsuit against someone. That was basically the substance of their assets. But he also said that at one time American Leisure had had assets and that he himself had purchased an interest in American Leisure Corporation. He may have, to the best of my recollection, personally owned 50,000 shares of American Leisure Corporation.

Q. Did he indicate or say at what point these assets had been owned by American Leisure? A. It was prior to his conversations with Mr. Lipsitz concerning American Leisure establishing a relationship with Tri-State Energy.

* * *

[1394] Q. Now, did Mr. Rubin tell you anything about the stock of companies called Satellite Systems and Marlin Investment? A. Yes, he did. Mr. Rubin said that Tri-State Energy came to rent shares of Satellite Systems and Marlin Investments from—through negotiations with an attorney by the name of William Hamilton, who represented and worked with a person by the name of Peter Crosby.

After the negotiations for the rent of these securities, they were delivered to Tri-State Energy's offices, according to Mr. Rubin, by a Mr. Benjamin. He indicated that Satellite securities were listed in the Herald-Tribune European edition of the newspaper, and to the best of my recollection, Mr. Rubin said that both of these securities were registered in the name of Bachelor Investments and that Bankers Trust Company tried to have these shares transferred into their nominee's name, and that they were not able to do this.

Q. That was what Mr. Rubin told you? A. That's what Mr. Rubin said. Mr. Rubin said [1395] to the best of my recollection, the rental fee for these shares was 7½ per cent of the market value, or if they were sold, to the best of my recollection he said the price would be one-half of the bid price.

Q. Now, this word "rental" whose word is that? A. To the best of my recollection, that's Mr. Rubin's word.

Q. Now, as someone with experience in the SEC, are you familar with the concept of renting stock? A. Yes.

Q. And can you tell us what it means to rent stock? A. Well, if you wanted to—if you thought a stock would depreciate in value from its current price, you might want to borrow that stock from someone who owned it to sell it, and to buy it back at lower price and pay back that individual.

For the purpose of borrowing the stock, you would pay the lender a fee.

Q. And it remains the lender's stock, is that correct? A. It remains the lender' stock, and you can return the identical stock to the lender or the equivalent of that stock.

Q. In other security or whatever? [1396] A. It depends on the arrangement you would make with the lender. Normally speaking, you would return the stock in kind, not necessarily the same certificate, but you would return the stock in kind. It is possible to return, depending on your agreement with the lender, a stock of equivalent value.

The Court: Read that answer.

(Answer read.)

The Court: I don't understand that. Could you explain that in simpler language?

The Witness: I will try.

The Court: Buy it back at a lower price?

The Witness: Actually, what I am explaining is probably more akin to making what is called a short sale, which is selling a stock at one price in hopes of buying it back at a lower price, making a profit on the difference. In actual practice that's one way—one purpose for borrowing the stock, but also you could borrow a stock for any other purpose, to use as collateral for a loan, to use as part of your assets, or temporary business purposes.

It is almost like borrowing anything else of value, and normally speaking, when you borrow something of value, you have to pay something for it.

[1397] The Court: And you would borrow it and sell it and then buy it back?

The Witness: In a short sale, that's what you would do. You would borrow it, sell it, and then hopefully buy it back at a lower price, but for ordinary business purposes you could borrow it and use it as collateral for a loan or use it to have it appear on your balance sheet to make your assets appear to be greater, for cosmetic purposes you might say.

[1398] Q. Let's see if we can illustrate that first.

First, the one that's more like a short sale, if you borrowed a stock that was then $10— A. Yes.

Q. —you would hope to sell it at 10 or more, buy it from someone in the market or whatever at less than $10— A. If your expectations were realized and the stock appreciated in value, you could buy. If you sell 100 shares at

10 and buy it back at 5, return the 100 shares to the owner, your profit would be $5 minus or $500 minus your rental fee.

Q. Now, after the stock Marlin and Satellite was obtained pursuant to thes rental agreement, did Mr. Rubin tell you of any subsequent conversations involving Mr. Hamilton, Crosby or Benjamin? A. Yes, he did.

Q. Do you recall what that was? A. Yes, I do.

Mr. Rubin said he received at Tri-State Energy's offices several calls from Mr. Hamilton and from Mr. Crosby wanting to know where the money was, their rental fee for the Marlin Investments and Satellite Systems.

Q. And that was the telephone call? A. Telephone calls. And he said that Mr. Benjamin [1399] made a personal appearance at Tri-State Energy's offices requesting the rental fee.

Q. As part of the same effort to get the rental fee? A. As part of the same effort to get the rental fee and at this point when Mr. Benjamin came to the office, Mr. Deaton was not there, acoerding to Mr. Rubin, Mr. Deaton was in Florida, and Mr. Rubin—to the best of my knowledge, either Mr. Rubin was instructed to tell Mr. Benjamin or he told Mr. Benjamin on his own behalf that Satellite Systems and Marlin had not been used for loan collateral purposes.

* * *

[1401] Q. Do you recall Mr. Rubin telling you anything about substitution of collateral in Bankers Trust? A. Yes, I do.

Mr. Rubin said that two former members of the staff of North American Planning Corporation arranged for Tri-State Energy to purchase—to the best of my knowledge it was 100 thousand shares of a publicly owned

company, at a cost of $100 thousand plus a $40 thousand commission. He said that these shares were placed with Bankers Trust Company as collateral for their loans and that shortly thereafter, the president of the issuing company of these shares requested that the shares be returned to the company, and the president [1402] of this company also made a request to the Securities and Exchange Commission that they suspend trading in the shares of his company because he could not determine the number of shares that were outstanding.

Mr. Rubin said that these shares were returned to the company and that the president returned to Tri-State Energy $100 thousand. He said that efforts were made by Tri-State Energy to obtain the $40 thousand but that the company declined, indicating that they were not concerned with the commission of $40 thousand.

Q. Did he tell you anything about substitute stock? A. Yes, he did. He said that these two individuals that had arranged to get this 100 thousand shares of publicly owned stock, arranged to obtain a substitute stock.

Q. Did he tell you whether that was ever paid for? A. May I refer to my notes?

Q. Certainly.

(Pause.)

A. After reviewing my notes, to the best of my knowledge, Mr. Rubin said that the stock that was used to replace the collateral was not paid for.

Mr. Bender: I didn't get that.
The Court: Read the answer.

(Record read.)

[1403] Mr. Bender: May we ask what note, particular notes he reviewed for that recollection to be refreshed?

The Witness: These are the notes of February 14, 1975.

Mr. Bender: Thank you.

A. (Continuing) Mr. Rubin said that the stock was not paid for and that after a few weeks persons described as "hard guys" paid a visit to the offices of Tri-State Energy.

Mr. Bender: I move to strike that, your Honor.

The Court: Is this something that Mr. Rubin said?

Mr. Bender: But, even if he did—even if he says he did say it, I think it is totally irrelevant, inconsistent and it can give a wrong impression.

Ms. Neugarten: Your Honor—

The Court: Well, yes?

Ms. Neugarten: The testimony I believe of Mr. Keating was that he was told that the stocks were always obtained by swapping coal rights, and I think the government is entitled to prove through various of Mr. Rubin's statements whether that was a correct or a false representation as made to Mr. Keating.

The Court: I see.

[1404] Mr. Bender: I have no objection to trying to prove through any admissions something that's material to what Mr. Keating said, but I think the use of words "hard guys," I mean, why should we be afflicted with the inferences that can be drawn

from that kind of description? I don't think really it belongs in the case.

The Court: Is this choice of words Mr. Rubin's?

The Witness: Your Honor, I have written here "hard guys."

Mr. Bender: Just a moment, please.

The Court: The question is, are those words Mr. Rubin's?

The answer to that is yes or no. Are those words, "hard guys," something Mr. Rubin said?

The Witness: To the best of my recollection, your Honor, those are the words that Mr. Rubin used.

* * *

[1490] Ms. Neugarten: With Mr. Bender's permission, rather than read out the words of the exhibits, I would like to simply indicate that as to 151 through 156, as to companies whose names I will read from the exhibits, they indicate that a diligent search has been made of records of the Securities and Exchange Commission and there has been no record found of any registration of the stock of those companies.

If you think that is an unfair summary—

Mr. Bender: No, that will be fine.

Ms. Neugarten: The names of the companies are for 151, Management Dynamics, Inc.

152, Management Dynamics Incorporated, written out.

153, Marlin Investment Company.

154, All States Life Insurance Company.

155, Satellite Systems Corporation.

156, American Leisure Corporation.

Now, as to 157, which does indicate something [1491] was done or found, I will read simply what was found and not the certification of the certifying official.

A registration statement on Form 15 for Incorporated Investment Companies was filed with this Commission July 31, 1935, by General Investment Corporation pursuant to the provisions of the Securities Exchange Act of 1934 via 1/1/1953.

A registration statement on Form 23 for successor issuers was filed with this Commission October 10, 1944, by General Investment Corporation, pursuant to the provisions of the Securities Exchange Act of 1934, filed 1/31/59.

I further attest that a diligent search has this day, May 2, 1978, been made of the books and records of this Commission and the books and records do not disclose that any registration statement other than the ones described above have been filed with this Commission under the name General Investment Corporation pursuant to the provisions of any of the Acts administered by this Commission.

* * *

William Robert Rubin—Petitioner—Direct

[1774] WILLIAM ROBERT RUBIN, called as a witness on his own behalf, having first been duly sworn, testified as follows:

(Direct Examination)

* * *

[1920] I didn't even sign all the notes.

Q. Did you sign a confession of judgment, acknowledging the debt? A. Yes, I did. And I signed a confession of judgment. I certainly did; for over a half million dollars, to be precise, with interest added, and attorneys' fees added.

Ms. Neugarten: Mark these, please.

(Government's Exhibits 163 and 164 were marked for identification.)

Q. I am handing you what have been marked as Government's Exhibits 163 and 164 for identification. Do these appear to be, in the case of 163, a photocopy of an affidavit of confession of judgment, on a so-called Blumberg form; and 164, a letter acknowledged by you, as to your debt as to Bankers Trust? A. Yes.

Q. Both documents bear your signature? A. Yes.

Ms. Neugarten: At this time the government offers Exhibits 163 and 164 for identification into evidence.

Mr. Bender: I have no objection, your Honor.

* * *

William Robert Rubin—Petitioner—Cross

(Cross Examination)

[2077] Q. Do you recall being asked on Friday both in direct examination and cross-examination regarding conversations you had with Mr. Pinto and representatives of the SEC concerning All States stock? A. Yes.

Q. Is it your testimony that at no time did either Mr. Pinto, a Mr. Pilpel, or anyone else from the NSAD ever tell you that the All States stock might be restricted? [2078] A. I don't remember Mr. Pilpel but I remember Mr. Pinto very well. I believe it was my testimony that they felt that the stock was thinly traded. At that particular time I do not recall them telling me about anything being restricted. They might have said that there is a question, but I don't know if I was ever directly, specifically, told that that is restricted stock.

Q. They might have said there was a question as to whether it was restricted? A. They might have. It could have been a question in everyone's minds.

Q. You understood there was a question whether it might not in fact be restrictive, is that correct? A. That's not absolutely correct.

Q. You had some familiarity with the laws and the rules governing controlled stock, is that correct? A. Yes.

Q. You understood that a substantial block would be very apt to be restricted stock? A. Unless there was a shelf registration or something like that. There might have been a suspicion, but it was not fact at that time. I could have suspected it.

• • •

Government Exhibit 1

30 Day Promissory Note for $50,000, dated October 20, 1972

[PHOTOSTAT]

(Opposite) ☛

301.38 49698.62

$ 50,000 — New York, N. Y., OCT 20 19 71

ONE (1) MONTH after date, for value received, the undersigned promises to

pay to the order of BANKERS TRUST COMPANY 1-102

FIFTY THOUSAND AND 00/100 Dollars

at the office of BANKERS TRUST COMPANY at NEW 27TH AVE, N. Y.

Upon non-payment when due of this note or of any of the other liabilities of the undersigned, or if it appears at any time that any representation in any financial or other statement of the undersigned, delivered to the Bank by or on behalf of the undersigned, is untrue or incomplete, or if an adverse change shall occur in the financial condition of the undersigned, or if the undersigned or any endorser or guarantor of this note shall die or (being a partnership or corporation) shall be dissolved, or shall become insolvent (however evidenced), or upon the suspension of business of the undersigned, or upon the issuance of any warrant, process, or order of attachment, garnishment or other lien and/or the filing of a lien as a result thereof against any of the property of the undersigned, or upon the commencement of any proceeding under, or the use of any of the provisions of, Article 52 of the New York Civil Practice Law and Rules by any judgment creditor against the undersigned or with respect to any property of the undersigned, or upon the making by the undersigned or any endorser or guarantor of this note of an assignment for the benefit of creditors, or upon a trustee or receiver being appointed for the undersigned or any endorser or guarantor of this note or for any of the property thereof, or upon any proceedings being commenced by or against the undersigned or any such endorser or guarantor under any bankruptcy, reorganization, arrangement of debt, insolvency, readjustment of debt, receivership, liquidation or dissolution law or statute, — then and in any such event, all liabilities of the undersigned shall become at once due and payable, without notice, presentment or demand of payment, which are hereby expressly waived. No delay on the part of the Bank in exercising any of its options, powers or rights, or partial or single exercise thereof, shall constitute a waiver thereof. If this note is not paid when due, the undersigned and each endorser each agrees to pay interest on the unpaid balance at the maximum rate of interest permitted by law and all costs and expenses of collection including attorneys' fees of 15% of the unpaid balance of the loan evidenced hereby. The undersigned, if more than one, shall be jointly and severally liable hereunder and the term "undersigned" wherever used herein shall mean the undersigned or any one or more of them.

Due 11/20

4 1 7 9 4 9 3 5

Insert your Bankers Trust Company checking account number here

23917 710

Jeff Deaton Sec. & Treas.

E. S.

F2137—ABC 4-71

Government Exhibit 7
Blank Stock Power

[PHOTOSTAT]

(Opposite ☛)

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

(_____) *Shares of the* _____ *Capital Stock of* _____

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated _____

TRI-STATE ENERGY, INC.

C. W. Deaton

C.W. Deaton, Secretary-Treasurer

In presence of

_____

CHELSEA NATIONAL BANK
SIGNATURE GUARANTEED

ASSISTANT VICE PRESIDENT

7

Government Exhibit 8

Blank Stock Power

[PHOTOSTAT]

(Opposite) ☛

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

(_____) *Shares of the* _____ *Capital Stock of* _____

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated _____

TRI-STATE ENERGY, INC.

C. W. Dean

C.W. Dean, Secretary-Treasurer

In presence of

_____

CHELSEA NATIONAL BANK
SIGNATURE GUARANTEED

ASSISTANT VICE PRESIDENT

8

Government Exhibit 11

3 Month Promissory Note for $50,000, dated November 20, 1972

[PHOTOSTAT]

(Opposite) ☛

694.44 49 105.51

$ 50,000—

New York, N. Y., NOV 20 19 72

THREE (3) MONTHS after date, for value received, the undersigned promises to

pay to the order of BANKERS TRUST COMPANY

FIFTY THOUSAND AND 00/100 Dollars

at the office of BANKERS TRUST COMPANY at 280 PARK AVE, N. Y.

Upon non-payment when due of this note or of any of the other liabilities of the undersigned, or if it appears at any time that any representation in any financial or other statement of the undersigned, delivered to the Bank by or on behalf of the undersigned, is untrue or incomplete, or if an adverse change shall occur in the financial condition of the undersigned, or if the undersigned or any endorser or guarantor of this note shall die or (being a partnership or corporation) shall be dissolved, or shall become insolvent (however evidenced), or upon the suspension of business of the undersigned, or upon the issuance of any warrant, process, or order of attachment, garnishment or other lien and/or the filing of a lien as a result thereof against any of the property of the undersigned, or upon the commencement of any proceeding under, or the use of any of the provisions of, Article 52 of the New York Civil Practice Law and Rules by any judgment creditor against the undersigned or with respect to any property of the undersigned, or upon the making by the undersigned or any endorser or guarantor of this note of an assignment for the benefit of creditors, or upon a trustee or receiver being appointed for the undersigned or any endorser or guarantor of this note or for any of the property thereof, or upon any proceedings being commenced by or against the undersigned or any such endorser or guarantor under any bankruptcy, reorganization, arrangement of debt, insolvency, readjustment of debt, receivership, liquidation or dissolution law or statute, — then and in any such event, all liabilities of the undersigned shall become at once due and payable, without notice, presentment or demand of payment, which are hereby expressly waived. No delay on the part of the Bank in exercising any of its options, powers or rights, or partial or single exercise thereof, shall constitute a waiver thereof. If this note is not paid when due, the undersigned and each endorser each agrees to pay interest on the unpaid balance at the maximum rate of interest permitted by law and all costs and expenses of collection including attorneys' fees of 15% of the unpaid balance of the loan evidenced hereby. The undersigned, if more than one, shall be jointly and severally liable hereunder and the term "undersigned" wherever used herein shall mean the undersigned or any one or more of them.

Due 4 1 7 9 4 9 3 5

25123 Insert your Bankers Trust Company checking account number here

BANKERS TRUST COMPANY 1-10.3 CAPITAL

TREAS

F2137—ABC 4-71

Government Exhibit 12,

3 Month Promissory Note for $50,000, dated November 22, 1972, Extending the October 20, 1972 Note for 3 Months

[PHOTOSTAT]

(Opposite) ☛

$ 50,000 00/100

New York, N. Y., Nov 22 1972

3 months after date, for value received, the undersigned promises to pay to the order of BANKERS TRUST COMPANY

Fifty Thousand 00/100 Dollars

at the office of BANKERS TRUST COMPANY at 15 E 57th Street, N. Y.

Upon non-payment when due of this note or of any of the other liabilities of the undersigned, or if it appears at any time that any representation in any financial or other statement of the undersigned, delivered to the Bank by or on behalf of the undersigned, is untrue or incomplete, or if an adverse change shall occur in the financial condition of the undersigned, or if the undersigned or any endorser or guarantor of this note shall die or (being a partnership or corporation) shall be dissolved, or shall become insolvent (however evidenced), or upon the suspension of business of the undersigned, or upon the issuance of any warrant, process, or order of attachment, garnishment or other lien and/or the filing of a lien as a result thereof against any of the property of the undersigned, or upon the commencement of any proceeding under, or the use of any of the provisions of, Article 52 of the New York Civil Practice Law and Rules by any judgment creditor against the undersigned or with respect to any property of the undersigned, or upon the making by the undersigned or any endorser or guarantor of this note of an assignment for the benefit of creditors, or upon a trustee or receiver being appointed for the undersigned or any endorser or guarantor of this note or for any of the property thereof, or upon any proceedings being commenced by or against the undersigned or any such endorser or guarantor under any bankruptcy, reorganization, arrangement of debt, insolvency, readjustment of debt, receivership, liquidation or dissolution law or statute, — then and in any such event, all liabilities of the undersigned shall become at once due and payable, without notice, presentment or demand of payment, which are hereby expressly waived. No delay on the part of the Bank in exercising any of its options, powers or rights, or partial or single exercise thereof, shall constitute a waiver thereof. If this note is not paid when due the undersigned and each endorser each agrees to pay interest on the unpaid balance at the maximum rate of interest permitted by law and all costs and expenses of collection including attorneys' fees of 15% of the unpaid balance of the loan evidenced hereby. The undersigned, if more than one, shall be jointly and severally liable hereunder and the term "undersigned" wherever used herein shall mean the undersigned or any one or more of them.

Due 11/22/73

4	1	7	9	4	9	3	5

Insert your Bankers Trust Company checking account number here

25122

F2137—ABC 4-71

Government Exhibit 14

3 Month Promissory Note for $100,000, dated November 30, 1972

[PHOTOSTAT]

(Opposite) ☛

$ 100,000 00/100 — 90 — 1.1.72 — 98250.01

New York, N.Y., November 30 1972

3 months after date, for value received, the undersigned promises to pay to the order of BANKERS TRUST COMPANY One Hundred Thousand 00/100 Dollars

at the office of BANKERS TRUST COMPANY at 500 7th Ave, N. Y.

Upon non-payment when due of this note or of any of the other liabilities of the undersigned, or if it appears at any time that any representation in any financial or other statement of the undersigned, delivered to the Bank by or on behalf of the undersigned, is untrue or incomplete, or if an adverse change shall occur in the financial condition of the undersigned, or if the undersigned or any endorser or guarantor of this note shall die or (being a partnership or corporation) shall be dissolved, or shall become insolvent (however evidenced), or upon the suspension of business of the undersigned, or upon the issuance of any warrant, process, or order of attachment, garnishment or other lien and/or the filing of a lien as a result thereof against any of the property of the undersigned, or upon the commencement of any proceeding under, or the use of any of the provisions of, Article 52 of the New York Civil Practice Law and Rules by any judgment creditor against the undersigned or with respect to any property of the undersigned, or upon the making by the undersigned or any endorser or guarantor of this note of an assignment for the benefit of creditors, or upon a trustee or receiver being appointed for the undersigned or any endorser or guarantor of this note or for any of the property thereof, or upon any proceedings being commenced by or against the undersigned or any such endorser or guarantor under any bankruptcy, reorganization, arrangement of debt, insolvency, readjustment of debt, receivership, liquidation or dissolution law or statute, — then and in any such event, all liabilities of the undersigned shall become at once due and payable, without notice, presentment or demand of payment, which are hereby expressly waived. No delay on the part of the Bank in exercising any of its options, powers or rights, or partial or single exercise thereof, shall constitute a waiver thereof. If this note is not paid when due, the undersigned and each endorser each agrees to pay interest on the unpaid balance at the maximum rate of interest permitted by law and the costs and expenses of collection including attorneys' fees of 15% of the unpaid balance of the loan evidenced hereby. The undersigned, if more than one, shall be jointly and severally liable hereunder and the term "undersigned" wherever used herein shall mean the undersigned or any one or more of them.

Due — 4 1 7 9 4 9 3 5 — 2/28

Insert your Bankers Trust Company checking account number here

25195

RECEIVED PAYMENT
LOAN DEPT.
FEB 28

ENDORSEMENT GUARANTEED
BANKERS TRUST COMPANY
NEW YORK

14

F2137—ABC 4-71

Government Exhibit 16

3 Month Promissory Note for $275,000, dated December 6, 1972

[PHOTOSTAT]

(Opposite) ☛

$ 225,000.00 / 4814.94 / 220187.51

New York, N. Y., December 6 1972

3 months after date, for value received, the undersigned promises to pay to the order of BANKERS TRUST COMPANY Two Hundred Seventy Five Thousand 00/100 Dollars

at the office of BANKERS TRUST COMPANY at 550 5th Ave., N. Y.

Upon non-payment when due of this note or of any of the other liabilities of the undersigned, or if it appears at any time that any representation in any financial or other statement of the undersigned, delivered to the Bank by or on behalf of the undersigned, is untrue or incomplete, or if an adverse change shall occur in the financial condition of the undersigned, or if the undersigned or any endorser or guarantor of this note shall die or (being a partnership or corporation) shall be dissolved, or shall become insolvent (however evidenced), or upon the suspension of business of the undersigned, or upon the issuance of any warrant, process, or order of attachment, garnishment or other lien and/or the filing of a lien as a result thereof against any of the property of the undersigned, or upon the commencement of any proceeding under, or the use of any of the provisions of, Article 52 of the New York Civil Practice Law and Rules by any judgment creditor against the undersigned with respect to any property of the undersigned, or upon the making by the undersigned or any endorser or guarantor of this note of an assignment for the benefit of creditors, or upon the application for, consent to, or acquiescence in the appointment of a receiver being appointed for the undersigned or any endorser or guarantor of this note or for any of the property thereof, or upon any proceedings being commenced by or against the undersigned or any such endorser or guarantor under any bankruptcy, reorganization, arrangement of debt, insolvency, readjustment of debt, receivership, liquidation or dissolution law or statute, — then and in any such event, all liabilities of the undersigned shall become at once due and payable, without notice, presentment or demand, all of which are hereby expressly waived. No delay on the part of the Bank in exercising any of its options, powers or rights, or partial or single exercise thereof, shall constitute a waiver thereof. If this note is not paid when due, the undersigned and each endorser each agrees to pay interest on the unpaid balance at the maximum rate of [illegible] per annum permitted by law and all costs and expenses of collection including attorneys' fees of 15% of the unpaid balance of the loan evidenced hereby. The undersigned, if more than one, shall be jointly and severally liable hereunder and the term "undersigned" wherever used herein shall mean the undersigned or any one or more of them.

RECEIVED PAYMENT
LOAN DEPT.
DEC 8 1972
ENDORSEMENT GUARANTEED
BANKERS TRUST COMPANY
NEW YORK

Due 25650

4 1 7 9 4 9 3 5

Insert your Bankers Trust Company checking account number here

3 / 15 - STATE ENERGY INC. 16

F2137—ABC 4-71

Government Exhibit 19, Power of Attorney

POWER OF ATTORNEY

TO ENDORSE SECURITIES

KNOW ALL MEN BY THESE PRESENTS, that

I, ...
(Name)

residing at .....
(Address)

have made, constituted and appointed and by these presents do make, constitute and appoint BANKERS TRUST COMPANY, a New York corporation, my true and lawful attorney for me and in my name, place and stead and for my account and risk, with power to execute endorsements, assignments or other instruments of conveyance or transfer of certificates of stock or registered securities which it holds or may hold for me registered in my name, and to execute any necessary due bills, by signing my name only or by signing the same as my attorney in fact, as may be deemed by my said attorney to be necessary or desirable and proper in connection with the transfer of said securities.

IN WITNESS WHEREOF, I have hereunto set my hand and seal this 27th day of November 1972.

C. W. DEATON
C. W. Deaton (L.S.)
Treasurer

Government Exhibit 20, Corporate Resolution

CORPORATE RESOLUTION

TRANSFER OF SECURITIES

RESOLVED, that any.....of the following officers of this Corporation, to wit,

be and they hereby are authorized to sell, assign, transfer or dispose of any stocks, bonds or other securities now or hereafter owned or held by this Corporation.

I, C. W. Deaton secretary of Tri-State Energy Inc. hereby certify that the foregoing is a true copy of a resolution duly adopted by the Board of Directors of said Corporation at a meeting duly held the 7th day of December, 1972, at which a quorum was present, and that the same has not been repealed or amended and remains in full force and effect.

Dated: December 7th, 1972

C. W. DEATON

Secretary

Signature guaranteed by:

JOHN J. (Illegible)

(SEAL)

NOTE (1). The above form of resolution does not authorize a transfer into the individual name of any officer or director of the Corporation. Such a transfer must be specifically authorized by the Board of Directors.

NOTE (2). The signature of the officer certifying this resolution must be guaranteed by a commercial bank or trust company having a New York City corespondent, or by a member of the New York Stock Exchange.

Government Exhibit 21

Demand Note for $475.000, dated February 26, 1973

[PHOTOSTAT]

(Opposite) ☛

$475,000.00 New York, N. Y., February 26 1973

Demand after date, for value received, the undersigned promises to pay to the order of BANKERS TRUST COMPANY,

Four Hundred Seventy Five Thousand 00/100 Dollars

at the office of BANKERS TRUST COMPANY at 550 7th Ave., N. Y., and to pay interest on the unpaid principal amount hereof until maturity at the rate of 12 per cent. per annum payable on the _____ day of each month.

No. _____ Due _____

Tri-State Energy Inc

Leonard Jospin Pres.

(Please insert your Bankers Trust Company checking account number) 44 794 938

A.A. OTIER 25:19

F2139—4-71

Government Exhibit 28

Blank Stock Power

[PHOTOSTAT]

(Opposite) ☛

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

(_____) *Shares of the* _____ *Capital Stock of* _____

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated _____

_____

SIGNATURE GUARANTEED
NORTH AMERICAN PLANNING CORPORATION

In presence of

_____

SIGNATURE GUARANTEED
CHELSEA NATIONAL BANK

_____
Authorized Signature

28

Government Exhibit 29

Blank Stock Power

[PHOTOSTAT]

(Opposite) ☛

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

(_____) *Shares of the* _____ *Capital Stock of* _____

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated _____

_____

SIGNATURE

NORTH AMERICAN [illegible]

_____

SIGNATURE GUARANTEED

CHELSEA NATIONAL BANK

In presence of

_____

29

_____

Authorized Signature

Government Exhibit 30, Tri-State Energy Corporate Resolution, June 28, 1972

TRI-STATE ENERGY INC.
208 EAST MAIN STREET
WHITESBURG, KENTUCKY
ZIP: 41858

RESOLVED: That this is a duly authorized called meeting.

RESOLVED: That Leonard James, President, and/or C.W. Deaton, Secretary-Treasurer, are hereby authorized to sign any and all papers necessary to cause to be arranged a loan on ALL STATES INSURANCE COMPANY of ALABAMA stock.

Further be RESOLVED: That they, acting in their DULY elected offices, are authorized to do whatever is required to perfect such a loan, or loans.

IN WITNESS WHEREOF, I have hereunto set my hand as Secretary of said Corporation, and affixed the Corporation Seal this June 28, 1972.

TRI-STATE ENERGY, INC.
C. W. DEATON
Secretary-Treasuer

LEONARD JAMES
Pres.

CHELSEA-NATIONAL BANK
Signature Guaranteed
(ILLEGIBLE)
Assistant Vice President

Government Exhibit 37A

Stock Power

[PHOTOSTAT]

(Opposite) ☛

ERASURE GUARANTEED
BANKERS TRUST CO.

Authorized Signature

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____

TRI STATE ENERGY INC.

230 PARK AVE NEW YORK 10017

( ) *Shares of the* _____ *Capital Stock of* MARLIN INVESTMENT COMPANY

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). 1121/4 & 5412

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated 12/22/67

BACHELOR INVESTMENTS

_____

In presence of

Signature Guaranteed
CHEMICAL BANK
65th Street & Broadway
New York, N. Y.

_____

Authorized Signature

37A

Government Exhibit 37B
Undated Stock Power

[PHOTOSTAT]

(Opposite) ☛

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

(_____) *Shares of the* _____ *Capital Stock of* MARLIN INVESTMENT COMPANY

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on the books of said Corporation with full power of substitution in the premises.

Dated _____

BACHELOR INVESTMENTS

_____

Signature Guaranteed
CHEMICAL BANK
65th Street & Broadway
New York, N. Y.

In presence of

_____

37B

_____

Authorised Signature

©

Government Exhibit 37C
Undated Stock Power

[PHOTOSTAT]

(Opposite) ☛

STOCK POWER

FOR VALUE RECEIVED, _____

PLEASE INSERT SOCIAL SECURITY OR OTHER IDENTIFYING NUMBER OF ASSIGNEE

hereby sell, assign and transfer unto _____ _____

_____

_____

MARLIN INVESTMENT COMPANY

(_____) Shares of the _____ *Capital Stock of* _____

_____ *standing in my(our) name(s)*

on the books of said Corporation represented by Certificate(s) No(s). _____

herewith, and do hereby irrevocably constitute and appoint _____

_____ *attorney to transfer the*

said stock on thc books of said Corporation with full power of substitution in the premises.

BACHELOR INVESTMENTS

Dated _____

_____

Signature Guaranteed
CHEMICAL BANK
65th Street & Broadway
New York, N. Y.

37C

In presence of

_____

_____

Authorized Signature

Government Exhibit 38A, Undated Letter of Consent to Pledge Stock

LETTER OF CONSENT TO PLEDGE AND HYPOTHECATION

_____, N. Y.

_____, 19___

_____,

_____, New York

Dear Sirs:

The undersigned hereby certifies and agrees that Tri State Energy Inc. (hereinafter called the "borrower"), is authorized to pledge and hypothecate under the terms of your general loan and security agreement and/or security agreement note forms or otherwise, for the borrower's own account or otherwise, and the undersigned agrees that, when so pledged and hypothecated, the collateral (as hereinafter defined) shall secure, and that a security interest in the collateral and the proceeds thereof exist and will continue to exist in your favor as security for, any and all loans and/or advances at any time or from time to time made by you to the borrower, any present or future indebtedness or other obligations of the borrower to you, and all other indebtedness or other obligations, direct or indirect, absolute or contingent, due or to become due, now existing or hereafter arising, howsoever evidenced or acquired, and whether joint, several or joint and several, or independent of the borrower, and any renewals or extensions of any or all thereof (all being hereinafter called the "liabilities of the borrower"), the following described securities and/or personal property

Government Exhibit 38A

owned by the undersigned (hereinafter collectively called the "collateral"), to wit: 20,000 shares MARLIN INVESTMENT COMPANY.

The undersigned further certifies that the undersigned has good and valid legal title to the collateral, free and clear of all liens, charges, security interests, and incumbrances of any nature whatsoever.

You are hereby expressly authorized to accept and act upon any or all written instructions given to you either by the borrower or the undersigned regarding any sale or other dispositions of all or any part of the collateral, or any additions thereto, or substitutions therefor, or proceeds thereof, or any other collateral or security of the undersigned available to you, including deliveries or payments of the same or any part thereof, to or upon the order of either the borrower or the undersigned. Any additions, substitutions or proceeds of the collateral in any form whatsoever in the possession of either the undersigned or the borrower shall be held in trust for you.

The authorizations hereinbefore contained shall remain in full force and effect until receipt by you of written notice from the undersigned of the revocation or termination hereof; provided, however, that no revocation or termination hereof shall affect in any manner your rights arising hereunder with respect to liabilities of the borrower which shall have been created, contracted, assumed or incurred prior to receipt by you of written notice of such revocation or termination, or the liabilities of the borrower which shall have been created, contracted, assumed or incurred after receipt of such written notice pursuant to any agreement entered into by you prior to receipt of such written notice.

Government Exhibit 38A

The undersigned hereby agrees, for himself, his heirs, executors, legal representatives, successors and assigns, to hold you harmless in your reliance hereon, prior to your receipt of written notice of revocation or termination hereof, whether or not any or all the authorizations hereinbefore contained may theretofor have been terminated by operation of law or otherwise. Any action permitted hereby or under the terms and provisions of any instruments evidencing the liabilities of the borrower may be taken without notice to the undersigned. The undersigned hereby waives notice of default in the payment of any liabilities of the borrower, notice of sale or other realization upon the collateral or any part thereof, or any other notice or demand otherwise required to be given to or made upon upon the borrower or the undersigned by law, by the terms and provisions hereof, or by the terms and provisions of any instruments evidencing the liabilities of the borrower, or any notice or demand which you elect to give to or make upon the borrower.

No modifications or waiver of any of the provisions hereof shall be effective unless expressly stated in writing and signed for or on behalf of you and then only in the specific instance for which given. Each reference herein to the undersigned shall be deemed to include the undersigned's heirs, executors, legal representatives, successors and assigns.

Witness

(ILLEGIBLE)

(ILLEGIBLE)

Permanent Address

Government Exhibit 38A

(ILLEGIBLE)

(ILLEGIBLE)

Permanent Address

The undersigned, the borrower referred to in the foregoing agreement, hereby accepts notice of the execution and delivery thereof and of the terms and provisions thereof. The undersigned hereby agrees that you may at any time or from time to time accept payment from the person signing the foregoing agreement of all or any part of the liabilities of the borrower, as defined in the foregoing agreement, and/or transfer or assign any or all instruments evidencing such liabilities of the borrower and the collateral securing the same to said person or to anyone else, all without recourse to or/warranty by you. Any action permitted hereby or under the terms and provisions of the foregoing agreement or of any instruments evidencing said liabilities of the borrower may be taken without notice to the undersigned.

Witness

Permanent Address

(L.S.)

Permanent Address

Government Exhibit 47, Draft Memo of Bankers Trust Company, dated December 6, 1972

December 6, 1972

Tri-State Energy Inc.
230 Park Avenue
New York, New York 10017

NEW ACCOUNT

The subject was incorporated in the State of Kentucky in June, 1972 to engage in the exploration and production of natural resources in the energy field. It has a mineral interest in 9,800 acres of land which engineering reports indicate contain approximately twenty million tons of coal. The firm is in the process of auger and strip-mining these reserves in conformity with Federal and State reclamation statutes.

In addition to the coal mining operation, Tri-State has controlling interest (72%) in American Leisure Corp., an OTC traded holding company, which in turn owns 80% of General Oil and Gas Inc., a public utility operating in the State of Tennessee. The other 20% of General Oil is directly owned by Tri-State Energy. General Oil and Gas has approximately 330 billion cubic ft. of natural gas, which at today's price would have a recoverable value of $250MM. Our entree to the firm was through William Rubin, Vice President, who was well and favorably known to us as an accountant with the firm of Fred Landau & Co., C.P.A.'s.

We have advanced $475M O/P supported by $750M in marketable securities as lien collateral. In the near future, we expect the lien collateral to be replaced by a guaranteed Letter of Credit which will be opened in our favor to sup-

Government Exhibit 47

port the loan. Financial statements do not reflect operating results, as the firm only recently processed its first sales of coal to Continental Coal Corporation and Repoca Resources. These sales are expected to net the firm after expenses, $340M over the next three months. General Oil and Gas has also been active in the natural gas operation and is shortly expected to sign a large contract with Anhaeuser Busch Inc. to supply gas for its breweries throughout the

We feel our confidence here is well placed, and expect this account to grow into a profitable and sizeable business in the near future.

JJK
RJL/JJK/gms

Government Exhibit 48, Draft Memo of Bankers Trust Company, dated January 11, 1973

MEMORANDUM FOR CREDIT FILE

Name Date 1/11/73

TRI-STATE ENERGY, INC.
230 Park Avenue
New York, New York 10017

NEW ACCOUNT

The subject was incorporated in the State of Kentucky in June 1972 and is engaged in the production and exploration of natural resources in the energy field. The firm owns the mineral royalty interest on approximately 24 million tons of coal located in Neon, Kentucky, and is in the process of auger and strip mining these resources in conformity with Federal and State reclamation statutes. We were introduced to the firm by William Rubin, Vice President, who was well and favorably known to us when he was an accountant with the firm of Fred Landau & Co., C.P.A.'s.

While the coal mining operation is Tri-State's primary function, it also has controlling interest (72%) in an OTC traded holding company named American Leisure Corporation. American Leisure Corporation's primary asset is an 80% interest in General Oil and Gas Inc., a public utility located in Tennessee. The remaining 20% of General Oil is directly owned by Tri-State Energy.

General Oil and Gas operates as a public utility in the transmission, transportation, purchase, and sale of natural gas and its byproducts. It has leases on natural gas lo-

Government Exhibit 48

cated under approximately 215,000 acres in Scott and Morgan Counties, Tennessee. According to an engineering survey, a copy of which we have on file, the probable reserves of natural gas located in the aforementioned acreage is 320 billion cubic ft. which at today's price would have a recoverable value of $250MM.

We have on file a copy of the October 20, 1972 balance sheet of Tri-State Enegery Inc. prepared by Englander and Bernstein, C.P.A.'s. The exhibit indicates cash of $250M, accounts receivable Charter Financial Ltd. $7500M and inventory of coal at sidings $180M to pay current debt of $3.7MM, including provision for Federal and State Income Taxes of $3.2MM on the above mentioned receivable from Charter Financial Ltd. In this connection, it should be pointed out that the receivable represents the sale of 2.5 million tons of coal at $3. per ton; in place, to Charter Financial Ltd. and guaranteed by Home Life Insurance Co. of New York. This receivable represents a signed contract although the actual sale is not expected to be consummated until the end of February, 1973.

Long term debt was $638M reflecting a 5% installment note of $608M payable to All State Life Insurance Co. over a 10 year period amortized in equal installments of $67.5M per year. As collateral for the loan, the insurance company has security interest in approximately 675 thousand tons of coal.

In addition to the current assets listed above, the statement reflects investments in All State Life Insurance $728M, Bank Computer Network $125M, and American Leisure Corp. $2.5MM for a total of $3407M. The balance sheet therefore indicates a working capital of $7650M and a net worth of $7191M. It should be noted that for state-

ment purposes, the mineral royalty interest in the firm's coal fields is carried at $1.

While we realize that the balance sheet adds little to the credit evaluation because of its obvious deficiencies, we have advanced $475M O/P supported by approximately $750M in marketable securities in a lien collateral. The company had requested a 100% advance on the collateral to which we refused. When the advances were made, certain primary factors entered into our reasoning, the largest being favorable regard for Mr. Rubin and his insistance that the cash flow of the firm represented by the sale to Charter Financial Ltd. plus the sale of coal outright to utilities and industrial users nationwide would enable the firm to retire the advance by the end of February. Our initial loan to the company was for $50M and our position was increased as the firm processed its first sale of coal to Continental Coal Corp. and Repoca Resources. In addition, we had private conversations with an engineer representing a large European firm who informed us that a Letter of Credit would shortly be opened in seven figure proportions to cover the sale of coal to his company. With this in mind, the remaining advances were made.

Tri-State Energy is now in the final process of negotiations with Ohio Gas Company on a $241M drilling contract covering the General Oil and Gas property in Tennessee. Of this $241M, approximately $100M per month will be paid the firm for its own use and will not be associated with this drilling program. Part of these funds will be used to retire our loan.

Additional information has recently caused us to re-evaluate our thinking on this credit. We were recently informed by William Powderly that an unresolved overdraft was

Government Exhibit 48

outstanding at the Chemical Bank. We had no knowledge that an account at Chemical existed when the account opened. A subsequent investigation at the Chemical Bank revealed that the account was overdrawn for approximately $12M and was caused by a check which was returned from a bank in Louisiana. Mr. Anderson, account officer of the Chemical Bank * * * (277 Park Avenue) stated that the entire matter had been forwarded to his Legal Department. A subsequent conversation with the principals of Tri-State revealed that they had thought that an O/P note for the amount of the overdraft was put on in October and had a maturity of 120 days. They stated that they had no reason to think anything different since they had had no correspondence or phone conversations with anyone from Chemical Bank regarding the overdraft since October. They indicated that they would be in touch with Chemical and have the matter resolved at once. In addition to this unpleasantness, the firm despite our $475M advance is still in a very tight cash position, and we have had occasion to return a number of checks over the past two weeks. Predicated on those two factors, we informed Tri-State that we expect our loans to be repaid on or prior to maturity, and that we would only reevaluate the firm's position after we had been completely repaid. As additional support for our loan, we have received an additional $1MM in marketable securities thus bringing our collateral picture to $1.7MM and giving us, what we feel, is adequate protection. In addition, we hold the personal guarantees of the three principals involved.

JJK
Raymond J. Ludwig/John J. Keating/gms
Seventh Avenue Office

cc: Mr. Powderly
Mr. Volen

Government Exhibit 49A-7, Memo from John J. Keating to W. C. Powderly, dated February 2, 1973

MEMORANDUM

February 2, 1973

To
Mr. W. C. Powderly
Vice President
280 Park Avenue 2W

Re: Tri-State Energy Inc.

Pursuant to your phone conversation with Ray Ludwig, the following is a list of the side collateral which we hold in support of our loan to the subject:

175,000 shares of General Investment Corporation

50,000 shares of Satellite Systems Corporation

20,000 shares of Marlin Investment Company

2,000 shares of All State Life Insurance Co. Inc.

400,000 shares restricted—American Leisure Corporation

JOHN J. KEATING/gms
Seventh Avenue Office

Government Exhibit 49A-8, Draft Memo of Bankers Trust Company, dated January 11, 1973

MEMORANDUM FOR CREDIT FILE

Name: Tri-State Energy, Inc
230 Park Avenue
New York, New York 10017

Date: 1/11/73

NEW ACCOUNT

The subject was incorporated in the State of Kentucky in June 1972 and is engaged in the production and exploration of natural resources in the energy field. The firm owns the mineral royalty interest on approximately 24 million tons of coal located in Neon, Kentucky, and is in the process of auger and strip mining these resources in conformity with Federal and State reclamation statutes. We were introduced to the firm by William Rubin, Vice President, who was well and favorably known to us when he was an accountant with the firm of Fred Landau & Co., C.P.A.'s.

While the coal mining operation is Tri-State's primary function, it also has controlling interest (72%) in an OTC traded holding company named American Leisure Corporation. American Leisure Corporation's primary asset is an 80% interest in General Oil and Gas Inc., a public utility located in Tennessee. The remaining 20% of General Oil is directly owned by Tri-State Energy.

General Oil and Gas operates as a public utility in the transmission, transportation, purchase, and sale of natural gas and its byproducts. It has leases on natural gas located under approximately 215,000 acres in Scott and Morgan Counties, Tennessee. According to an en-

gineering survey, a copy of which we have on file, the probable reserves of natural gas located in the aforementioned acreage is 330 billion cubic ft. which at today's price would have a recoverable value of $250MM.

We have on file a copy of the October 20, 1972 balance sheet of Tri-State Energy Inc. prepared by Englander and Bernstein, C.P.A.'s. The exhibit indicates cash of $250M, accounts receivable Charter Financial Ltd. $7500M and inventory of coal at sidings $180M to pay current debt of $3.2MM on the above mentioned receivable from Charter Financial Ltd. In this connection, it should be pointed out that the receivable represents the sale of 2.5 million tons of coal at $3. per ton, in place, to Charter Financial Ltd. and guaranteed by Home Life Insurance Co. of New York. This receivable represents a signed contract although the actual sale is not expected to be consummated until the end of February, 1973.

Long term debt was $638M reflecting a 5% installment note of $608M payable to All State Life Insurance Co. over a 10 year period amortized in equal installments of $67.5M per year. As collateral for the loan, the insurance company has security interest in approximately 675 thousand tons of coal.

In addition to the current assets listed above, the statement reflects investments in All State Life Insurance $782M, Bank Computer Network $125M, and American Leisure Corp. $2.5M for a total of $3407M. The balance sheet therefore indicates a working capital of $7650M and a net worth of $7191M. It should be noted that for statement purposes, the mineral royalty interest in the firm's coal fields is carried at $1.

Government's Exhibit 49A-8

While we realize that the balance sheet adds little to the credit evaluation because of its obvious deficiencies, we have advanced $475M O/P supported by approximately $750M in marketable securities in lien collateral. The company had requested a 100% advance on the collateral to which we refused. When the advances were made, certain primary factors entered into our reasoning, the largest being farovable regard for Mr. Rubin and his insistance that the cash flow of the firm represented by the sale to Charter Financial Ltd. plus the sale of coal outright to utilities and industrial users nationwide would enable the firm to retire the advance by the end of February. Our initial loan to the company was for $50M and our position was increased as the firm processed its first sale of coal to Continental Coal Corp. and Repoca Resources. In addition, we had private conversations with an engineer representing a large European firm who informed us that a letter of Credit would shortly be opened in seven figures proportions to cover the sale of coal to his company. With this in mind, the remaining advances were made.

This is a very fluid situation at the present time. The company is in the process of negotiations on many fronts either or all of which will enable the firm to repay our loan and become a substantial depositor coincidental with the repayment of their debt to us. In connection with General Oil and Gas Inc.'s operation, the following factors are of prime importance:

1. The firm is in the final process of negotiations with Ohio Gas Co. on a $24MM drilling contract covering their Tennessee properties. The proposed contract covers a two year period at $1MM per month of which $100M per month is not associated with the

drilling program, and which the firm may use for working capital purposes.

2. Tri-State has been negotiating with Anheuser Busch Inc. to supply natural gas to run its Columbus, Ohio plant. They are interested in participating with Tri-State in a drilling and supply program which would accrue the firm money well into seven figure proportions. Specific details on this deal will be forthcoming at the signing of the contract. The contract date should occur within the next six weeks.

Tri-State's coal operation will shortly commence selling to Louisville Power and Light at the rate of 10,000 tons per week high grade coal. The coal will be sold at the price of $15 per ton, the sale of which will place the firm's cash flow position on a more permanent basis (spot sales had been the rule of thumb prior to this time) and eliminate their very tight cash position. As stated previously, the sale of coal in place to Charter Financial Ltd., a Bahamanian organization should be consummated by the end of February, at which time the firm will receive an up front payment of $500M.

For the record, the firm continues in a very tight cash position, and we have had occasion to return a number of checks over the past few weeks. However, we believe this will be a short run situation with the above referenced factors eliminating the cash bind shortly. If none of the aforementioned alternative sources of funds materialize, we have suggested to the firm that they explore other sources of financing. Since our Mining Group is not interested in coal receipt financing, the firm has explored this possibility with the Energy Groups of the Bank of New York and First National City, both of whom appear

Government's Exhibit 49A-8

to be receptive. We hold the personal guaranties of all principals involved and feel satisfied to continue on the present basis until the maturity of our notes are reached. As further support for our loan, the firm has recently given us an additional $1MM in side collateral represented by 50,000 shares of Satellite Systems Corporation, traded on a London OTC exchange for approximately $20. Our total marketable side collateral position now stands at approximately $1.7MM and we feel that we have adequate protection even though we do not envision being forced to sell these stocks at this time. At maturity, a further evaluation of our position will be made.

JJK
Raymond J. Ludwig/John J. Keating/gms
Seventh Avenue Office

cc: Mr. Powderly
Mr. Volen

Government Exhibit 49B-7, Letter from Jack Lifsitz to William R. Rubin, dated October 27, 1972

AMERICAN LEISURE CORPORATION
230 Park Avenue
New York 10017 - (212) 686-8050

October 27, 1972

Mr. William R. Rubin
230 Park Avenue
New York, New York 10017

Dear Mr. Rubin:

This will inform you that I will instruct the transfer agent to remove the legend on the 50,000 shares of common stock that you own and deliver to you free and unencumbered shares.

Very truly yours,

JACK LIFSITZ
Jack Lifsitz
President

JL:glc

Government Exhibit 49-58

International Advice Re: Satellite Systems Corp.

[PHOTOSTAT]

(Opposite) ☛

ADVERTISEMENT

International Stock Market

EUROBONDS

STRAIGHTS

Aer Lingus 81	101½	102½
Alfa Romeo 77	101	Bid
Bendix Int. 79	102	103
Borg Warner 79	103¼	104¼
Celanese Int. 82	95¼	96¼
Chevron Overs. 80	98	99
Citroën 82	94¾	95¾
Conoco 86	102½	103½
Continental Oil 86	101¾	102¾
Cyanamid 80	90¼	91¼
De Beers 82	91¾	92¾
Esso 86	104¾	105¾
Ford Intl. 81	105½	106½
General Mills 86	102½	103½
Honda 81	100	101
Mitsubishi 73	99½	Bid
Mobil 85	96¼	97¼
Nippon Electric 81	99¾	Bid
N. Amer. Rockwell Int. 73	99¼	Bid
Olivetti 85	107	108
Otis Elevator 85	105½	106½
Philip Morris 86	103½	104½
Procter & Gamble 82	96½	97½
Renault 82	95	96
Siemens West. Fin 85	108	109
Sumitomo Chem. 79	99½	101

SHARES

Holiday Trailer Lodges Int.	U.S.$	18½	19¾
Unibe Holdings S.A.	S.Fr.	1420	1425
Satellite Systems Corp.	U.S.$	20	20½

For information regarding membership and/or listing contact:

International Stock Market

1 Bartholomew Close,

London E.C.1, England.

Telephone: (1-236-3972.

49B-58

Government Exhibit 57, Investment Letter, General Investment Stock

INVESTMENT LETTER

Dear Sirs:

Shares	Certificate #	Registered To
200,000	#498 Thru 527	Tri-State Energy Inc.

I hereby certify and warrant that the above described shares of your already issued common stock of General Investment Corp., 2¢ par value per share, being transferred to me, were acquired by me for my own personal account for investment without any intention at the time of purchase of selling or distributing all or any part of the same.

I agree that I will not sell or distribute any of such shares except which may be legally sold or distributed without registration under the Securities Act of 1933, as amended, and/or federal statutes, or such shares shall have been so registered and are qualified and an appropriate prospectus shall then be in effect.

In connection with the foregoing, I consent to your marking the stock transfer book to indicate this investment intent and the restrictions on transfer contemplated hereby and to your placing a stop transfer order against said shares until the conditions set forth herein shall have been met.

Illegible, V.P.

Witness: C.W. Deaton
Illegible

Government Exhibit 65

Bankers Trust Company Notes, dated April 16, 1975 Re: Stocks and Loans, Tri-State Energy Company

[PHOTOSTATS]

(Opposite) ☛

Tri State Energy Inc.

Date Made		Amount
10-20-72	Renewal	$50,000
11-22-72		$50,000
11-22-72		$50,000
11-30-72		$100,000
12-6-72		$275,000

2/26/73 — $475,000 - Demand Note

1-59

OD

MANAGEMENT DYNAMICS INC (RCD 12/6/72 RETURNED 12/19/72

	100 AA	-	General Investment Corp.
12/19/72 *	175 AA	-	Satellite Systems Corp
12/19/13 *	50 AA	-	Marlin Investment Company
1/30/73 *	1.591 20 AA	-	ALL State Life Insurance Co. Inc.
11/10/72	2 AA	-	American Leisure Corp
7/5/73 *	400 AA		

** Restricted Stock

We have not received a reply from ALL State Life Insurance Co. Inc. ~~the~~ Registrar as to wheather the stock is restricted or not.

** All of it except American Corp was not supposed to be restricted.

April 16, 1975

Judith Hicks

65-3
XXX

Government Exhibit 147, Pink Sheets—All States Life Insurance Co. Stock

ALL-STATES LIFE INSURANCE CO. — ALABAMA

"Pink Sheets" Listings:

October 1, 1972, through March 31, 1973

Date	*Name of Market Makers*	*Bid*	*Ask*
Oct. 23, 1972	Marshall Murray & Co., Inc.	—	—
Oct. 25, 1972	Marshall Murray & Co., Inc.	21	22
Oct. 27, 1972	Marshall Murray & Co., Inc.	21	22
Oct. 30, 1972	Marshall Murray & Co., Inc.	21	22
Oct. 31, 1972	Marshall Murray & Co., Inc.	—	—
Nov. 1, 1972	Marshall Murray & Co., Inc.	—	—
Nov. 2, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 3, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 6, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 8, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 9, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 10, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 13, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 14, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 15, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 16, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 17, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 20, 1972	Marshall Murray & Co., Inc.	21	22

Government Exhibit 147

Date	*Name of Market Makers*	*Bid*	*Ask*
Nov. 21, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 22, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 27, 1972	Marshall Murray & Co., Inc.	—	—
Nov. 28, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 29, 1972	Marshall Murray & Co., Inc.	21	22
Nov. 30, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 1, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 4, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 5, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 6, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 7, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 8, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 11, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 12, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 13, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 14, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 15, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 18, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 19, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 20, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 21, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 22, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 26, 1972	Marshall Murray & Co., Inc.	21	22

Government Exhibit 147

Date	*Name of Market Makers*	*Bid*	*Ask*
Dec. 27, 1972	Marshall Murray & Co., Inc.	21	22
Dec. 29, 1972	Marshall Murray & Co., Inc.	21	22
Jan. 2, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 3, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 4, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 5, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 8, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 9, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 10, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 11, 1973	Not In Sheets		
Jan. 12, 1973	Not In Sheets		
Jan. 15, 1973	Not In Sheets		
Jan. 16, 1973	Not In Sheets		
Jan. 17, 1973	Not In Sheets		
Jan. 18, 1973	Not In Sheets		
Jan. 19, 1973	Not In Sheets		
Jan. 22, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 23, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 24, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 26, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 29, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 30, 1973	Marshall Murray & Co., Inc.	21	22
Jan. 31, 1973	Marshall Murray & Co., Inc.	21	22

Government Exhibit 147

Date	*Name of Market Makers*	*Bid*	*Ask*
Feb. 1, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 2, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 5, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 6, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 7, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 8, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 9, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 13, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 14, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 15, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 16, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 20, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 21, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 22, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 23, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 26, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 27, 1973	Marshall Murray & Co., Inc.	21	22
Feb. 28, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 1, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 2, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 5, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 6, 1973	Marshall Murray & Co., Inc.	21	22

Government Exhibit 147

Date	*Name of Market Makers*	*Bid*	*Ask*
Mar. 7, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 8, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 9, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 12, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 13, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 14, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 15, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 16, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 19, 1973	Marshall Murray & Co., Inc.	21	22
Mar. 20, 1973	Marshall Murray & Co., Inc.	21	22
	A. T. Brod	—	—
Mar. 21, 1973	A. T. Brod	—	—
Mar. 22, 1973	Marshall Murray & Co., Inc.	21	22
	A. T. Brod	—	—
Mar. 23, 1973	Marshall Murray & Co., Inc.	21	22
	A. T. Brod	—	—
	Dishy Easton	—	—

Government Exhibit 163

Affidavit of Confession of Judgment

[PHOTOSTAT]

(Opposite) ☛

BEST COPY AVAILABLE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

Index No.

BANKERS TRUST COMPANY,

Plaintiff

against

WILLIAM R. RUBIN,

Defendant

AFFIDAVIT OF CONFESSION OF JUDGMENT

STATE OF NEW YORK
COUNTY OF NEW YORK } ss.:

WILLIAM R. RUBIN,

duly sworn, deposes and says; that deponent is

† (the ~~corporation and is duly authorized to make this affidavit on behalf of the corporate~~ defendant herein.

The defendant hereby confesses judgment herein authorizes entry thereof against defendant in the sum of $ 529,000.00.

Defendant resides at 2000 Linwood Avenue, Fe, New Jersey 07024
in the County of Bergen State of rsey . Defendant authorizes entry
of judgment in** New York County, New said residence address is not in New York State.

This confession of judgment is for a debt justly due to the plaintiff arising from the following facts:

(1) Claim based on a written Gua[rantee] TRI-STATE ENERGY, INC., presently indebted with interest from March 9, 1973, amount[ing] $508,250.00, no part of which has been [paid] yment of the obligations of aintiff in the sum of $475,000.00 3,250.00, making a total of ough due and duly demanded.

(2) Claim for $20,000.00, based on $10,000.00 each for monies loaned by [plaintiff] February 3, 1972, amounting to $750.00. which has been paid although due and [demanded] Promissory Notes in the sum of defendant, with interest then total of $20,750.00, no part of ded.

This affidavit, if made in connection with an [agreement] modities for any use other than a commercial or [business] price or cost is payable in two or more installments [and] the payment of an installment thereunder.

or the purchase for $1,500.00 or less of any com- on any plan of deferred payments whereby the d subsequent to the time a default occurred in

Sworn to before me this
12th day of October 19 73

Vera E. Hershkopf

VERA E. HERSHKOPF
Notary Public, State of New York
No. 31-4766750
Qualified in New York County
Commission Expires March 30, 1975

The name signed must be printed beneath

WILLIAM R. RUBIN

** If in a city court, insert name of city. If in the county of Westchester, strike out.
† Strike out matter in parentheses if defendant is individual.
* Insert words "to become" if debt is not yet due.

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Petitioner's Exhibit J, Minutes of First Board of Directors, Tri-State Energy Held July 7, 1972

MINUTES OF FIRST MEETING OF BOARD OF DIRECTORS OF TRI-STATE ENERGY, INC.

The first meeting of the Board of Directors of Tri-State Energy, Inc., was held at Whitesburg, Letcher County, Kentucky, on July 7, 1972, pursuant to call and waiver of notice.

The following Directors of the corporation were present, constituting a majority of the Board:

C.W. Deaton Jack Deaton

C.W. Deaton exhibited a waiver of notice of the meeting signed by Leonard James, director.

C.W. Deaton was chosen Chairman of the meeting and Jack Deaton was chosen Secretary of the meeting.

By-laws were presented to the meeting, which were read and unanimously approved.

The Chairman called for the nomination of officers and the following persons were unanimously elected to serve for the term provided in the by-laws:

Leonard James—President

C. W. Deaton—Executive Secretary and Treasurer

Jack Deaton—Manager

C. W. Deaton, Executive Secretary and Treasurer then took charge of the meeting and acted as Chairman and presented the following resolutions to the Board, which were unanimously carried:

Petitioner's Exhibit J

RESOLVED, That the First Security Bank of Whitesburg, Kentucky, and Bank of Whitesburg, Whitesburg, Kentucky would be the depository of the corporation's funds and the Secretary-Treasurer was authorized to pay all incorporation expenses and to order a corporate seal.

RESOLVED: That Jack Deaton should be and he is hereby authorized as the managing agent of the corporation, to write checks from time to time in amounts up to $5,000.00 per draft or check.

C. W. Deaton then presented a contract with Georgianna Coal Sales, Big H. Combs Coal Co., Inc. and Herman Combs, Jr., individually, for the mining of coal, which contract was made to Ben Harvey as second party, with authorization to assign same to the corporation and upon the exhibition of the assignment of all contract rights in the corporation, the Board of Directors unanimously agreed to accept said contract and the Secretary was directed to so inform the President of Georgianna Coal Sales, Big H. Combs Coal Co., Inc., and Herman Combs, Jr., individually of the assignment.

RESOLVED: That on the 9th day of June, 1972, C. W. Deaton, acting as trustee, assigned two and one half million tons of future production of coal to North American Planning Corporation, 230 Park Avenue, New York City, New York, and the Corporation recognizes and accepts said obligation and ratifies the same in every respect.

RESOLVED: That on the 9th day of June, 1972, C. W. Deaton, acting as trustee, assigned two and one half million tons of future production of coal to American Leisure, Inc., 230 Park Avenue, New York City, New York, and the corporation recognizes and accepts said obligation and ratifies the same in every respect.

Petitioner's Exhibit J

The Secretary-Treasurer then advised that $35,000.00, the amount set forth in the Articles, had been paid in and the corporation would issue shares as follows:

Leonard James	50 shares
C. W. Deaton	50 shares

Leonard James President

C. W. Deaton
Executive Secretary and Treasurer

Order Granting Certiorari

SUPREME COURT OF THE UNITED STATES

No. 79-1013

WILLIAM RUBIN, Petitioner

v.

UNITED STATES

Order Allowing Certiorari. Filed April 14, 1980

The petition for a writ of certiorari is granted limited to Question 1 presented by the petition.

No. 79-1013

In the Supreme Court of the United States

OCTOBER TERM, 1979

WILLIAM RUBIN, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

WADE H. MCCREE, JR.
Solicitor General

PHILIP B. HEYMANN
Assistant Attorney General

WADE S. LIVINGSTON
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Washington, D.C. 20530

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In the Supreme Court of the United States

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WILLIAM RUBIN, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the court of appeals (Pet. App. 1a-67a) is reported at 609 F.2d 51.

JURISDICTION

The judgment of the court of appeals was entered on September 6, 1979, and a petition for rehearing was denied on November 20, 1979. The petition for a writ of certiorari was filed on December 19, 1979. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether petitioner's pledge of stock as collateral for a loan was a "sale" of a security (a term defined by statute to include any disposition of an interest in a security for value) and was thus subject to the antifraud provision of Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a).

2. Whether the government was required under *Brady* v. *Maryland*, 373 U.S. 83 (1963), to disclose the criminal record of a co-conspirator who did not testify at petitioner's trial.

3. Whether the district court properly admitted into evidence certain interview notes after petitioner's counsel made extensive use of those notes to cross-examine a government witness.

STATUTES INVOLVED

Section 2(3) of the Securities Act of 1933, 15 U.S.C. 77b(3), provides in pertinent part:

> The term "sale" or "sell" shall include every contract of sale or disposition of a security or interest in a security, for value. The term * * * "offer" shall include every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value.

Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), provides:

> It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communica-

tion in interstate commerce or by the use of the mails, directly or indirectly—

> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

STATEMENT

Following a jury trial in the United States District Court for the Southern District of New York, petitioner was convicted on one count of conspiracy to engage in securities fraud (15 U.S.C. 77q(a)), fraud in a bank loan application (18 U.S.C. 1014), mail fraud (18 U.S.C. 1341), and wire fraud (18 U.S.C. 1343), in violation of 18 U.S.C. 371. He was sentenced to three years' imprisonment. The court of appeals affirmed.

The evidence adduced at trial established that petitioner participated in an elaborate scheme to obtain bank loans for a financially failing company, Tri-State Energy, Inc. ("Tri-State"), by use of material misrepresentations, false documents, and bribery, and by pledging worthless securities as collateral.

Beginning in October 1972, petitioner and two other officers of Tri-State sought to obtain loans for Tri-State from Bankers Trust Company (Tr. 665, 1368).[1] Petitioner was acquainted with Raymond Ludwig, the officer at Bankers Trust who was in charge of corporate loans, and arranged a meeting with him (Tr. 665, 1368). Initially, Ludwig stated that a loan could not be made because Tri-State could not adequately document its assets or earnings potential (Tr. 666-667, 1368-1369). As he left the bank, petitioner told Ludwig: "[I]f you can see your way clear to help us, we will take care of you" (Tr. 667).[2]

To assure Ludwig and the other bank officers about Tri-State's financial condition, petitioner helped to prepare a financial statement that was materially false and misleading (Tr. 667-669). The financial statement listed a $7.5 million account receivable as Tri-State's principal asset, and a copy of the contract that purported to reflect this receivable was attached to the statement (Tr. 344, 349). In fact, no such receivable existed and the signature on the contract was forged (Tr. 641-647). At petitioner's suggestion, this "asset" was balanced on the financial statement by a

---

[1] Two officers of Tri-State (Leonard James and C. W. Deaton) and two other co-conspirators were indicted along with petitioner. James was convicted at a separate trial. Deaton has not yet been tried.

[2] One witness recalled that a different Tri-State officer made this statement to Ludwig and that it was later reported to petitioner (Tr. 1369). In either event, petitioner knew that Ludwig had been offered a bribe in connection with the loan application.

fictitious tax liability (Tr. 668). In addition, the financial statement, as originally prepared, listed $200,000 in cash on hand, attributable to two undeposited and uncashed personal checks, and $64,000 in cash in bank accounts (Tr. 668-669). Petitioner observed that these cash items would look suspicious, and, at his urging, the items were consolidated and listed as cash on hand with no explanation (*ibid.*). Finally, the financial statement indicated that Tri-State owned coal worth $180,000, when, in fact, it owned far less than that amount (Tr. 157-158, 667-668, 1391-1392). After this false information was furnished to the bank, the bank approved an initial loan of $50,000 (Tr. 674-675).

Shortly thereafter, petitioner and the two other Tri-State officers agreed that Ludwig should be paid the promised bribe as soon as possible (Tr. 675, 1369-1370). Accordingly, petitioner cashed a check for $1,500 at his country club and gave the money to Ludwig (Tr. 676, 1371). Later, petitioner gave Ludwig an additional $2,500 and made two $500 payments to a second bank official who approved the Tri-State loan (Tr. 211, 218, 315-316, 678-679, 1372-1373).

During the next six weeks, Tri-State was able to borrow an additional $425,000 from the bank (Tr. 1130). Petitioner engaged in a number of fraudulent acts to convince the bank that the loan was secure and to persuade it not to call the loan. For example, petitioner gave a bank officer a written projection of Tri-State's revenues that indicated that Tri-State

would receive $540,000 in gross income (Tr. 365-366). In fact, this projected income was based in substantial part on non-existent business contracts (Tr. 1109-1115, 722-723).

Another method used to conceal Tri-State's precarious financial position was the pledge of nearly worthless stock as collateral for the loans. At the request of a bank officer, petitioner agreed that Tri-State would provide marketable securities as collateral (Tr. 246). Between October 1972 and January 1973, Tri-State pledged the stock of several companies as collateral and represented that these securities were owned by Tri-State and were freely marketable (Tr. 305-313). In fact, Tri-State did not own the stock but only "rented" the shares (Tr. 682-684, 1394-1395). The shares were not freely tradeable and had no current market (Tr. 1490-1491). Petitioner created the appearance that one stock was marketable by engaging in apparent purchase and sale transactions so that the name of the stock would appear in the daily listings of an over-the-counter brokerage firm (Tr. 686-688, 1269-1273). Tri-State also tried to create the appearance of marketability in another stock pledged as collateral by showing a bank officer a newspaper clipping indicating that the stock was trading for about $20 a share (Tr. 410-411). In fact, the clipping was not a stock quotation at all but rather was an advertisement placed at the request of Tri-State (Tr. 723). Later, when the lessor of this stock discovered that it had been pledged, he informed the bank officer that Tri-State did not own it and

that it was restricted (Tr. 420-421). The bank officer then called petitioner, who claimed that Tri-State had been defrauded by the lessor and that he would have his attorney look into the matter (Tr. 421-423).

Tri-State was unable to repay the loans as they matured and Bankers Trust was forced to consolidate the loans into a single demand note (Tr. 284, 286-288). The bank was able to recover only $2,500 of the $475,000 (plus interest and expenses) that Tri-State was obligated to repay (Tr. 1129).

DISCUSSION

1. The principal question raised in the petition for certiorari (Pet. 7-14) is whether Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), which prohibits fraud "in the offer or sale of any securities," extends to fraud in the pledge of securities. The district court correctly determined that fraud in the pledge of securities is prohibited by Section 17(a) (Tr. 1554-1555) and the court of appeals affirmed that disposition.[3] Nevertheless, in view of the conflict among the courts of appeals on this issue and the importance of the issue to the enforcement of the federal securities laws, the United

[3] This question was fully briefed by the parties in the court of appeals. Petitioner's contentions were summarily rejected by the court without discussion (Pet. App. 34a). The court of appeals appears to have relied on its earlier holding in *United States* v. *Gentile*, 530 F.2d 461, 466-467 (2d Cir.), cert. denied, 426 U.S. 936 (1976), that a pledge is a "sale" within the meaning of the Securities Act.

States does not oppose granting the petition on this question.[4]

The split among the courts of appeals is illustrated by a comparison of the decisions of the Second Circuit with those of the Fifth and Seventh Circuits. The Second Circuit, in the present case and in *United States* v. *Gentile*, 530 F.2d 461, 466-467 (2d Cir.), cert. denied, 426 U.S. 936 (1976), has held that a pledge of securities is a "sale" within the meaning of Section 17(a). The Fifth and Seventh Circuits have reached the opposite conclusion. *National Bank of Commerce* v. *All American Assurance Co.*, 583

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[4] Three years ago, this Court granted certiorari to resolve the related question whether a pledge of stock is a sale of a security under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b). *Bankers Trust Co.* v. *Mallis*, 431 U.S. 928 (1977). That statute defines "sale" to include "any contract to sell or otherwise dispose of" a security. Section 3(a)(14) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(14). The Court dismissed the petition as improvidently granted after the respondents during oral argument changed the theory upon which they sought affirmance. 435 U.S. 381 (1978).

There is also a conflict among the circuits on the question whether a pledge is a sale under Section 10(b). Compare *Mansbach* v. *Prescott, Ball & Turben*, 598 F.2d 1017, 1028-1030 (6th Cir. 1979), and *Mallis* v. *FDIC*, 568 F.2d 824, 828-830 (2d Cir. 1977), cert. dismissed, 435 U.S. 381 (1978) (pledge is a sale under Section 10(b)), with *Lincoln National Bank* v. *Herber*, 604 F.2d 1038, 1040-1044 (7th Cir. 1979), *National Bank of Commerce* v. *All American Assurance Co.*, 583 F.2d 1295, 1298-1300 (5th Cir. 1978), *Reid* v. *Hughes*, 578 F.2d 634, 638 (5th Cir. 1978), and *McClure* v. *First National Bank*, 497 F.2d 490, 495-496 (5th Cir. 1974), cert. denied, 420 U.S. 930 (1975) (pledge is not a sale under Section 10(b)).

F.2d 1295, 1298-1300 (5th Cir. 1978); *Lincoln National Bank* v. *Herber*, 604 F.2d 1038, 1040-1044 (7th Cir. 1979).

We believe that the Second Circuit's position is correct. As with other questions of statutory interpretation, the starting point for analysis is the language of the statute itself. *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, No. 77-1645 (Nov. 13, 1979), slip op. 4. A pledge, the Second Circuit noted in *Gentile*, falls within the literal definition of a "sale" contained in Section 2(3) of the Securities Act of 1933, 15 U.S.C. 77b(3), which includes "every contract of sale *or disposition of a security or interest in a security*, for value" (emphasis supplied). 530 F.2d at 466. Restricting the term "sale" to transactions in which title to a security passes "would render superfluous" the statutory language emphasized above. *Ibid.*

The banking context in which pledge transactions frequently occur does not require a different result. The antifraud provisions of the federal securities laws are not limited to protection of investors. See *United States* v. *Naftalin*, 441 U.S. 768, 772-777 (1979). They protect creditors as well. See *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 12 & n.8 (1971).

The antifraud provisions of the federal securities laws were intended to apply when any person is deceived into parting with money in exchange for an interest in a security. As the Second Circuit has explained, "there is no reason to doubt that Congress

intended [the Securities] Act to protect defrauded lenders just as much as defrauded buyers," because pledgee-lenders, like investors, assume "a very real investment risk that the pledged securities will have continuing value." *United States* v. *Gentile*, *supra*, 530 F.2d at 467.[5] Petitioner's contrary interpretation "would create a loophole in the statute that Congress simply did not intend to create" (*United States* v. *Naftalin*, *supra*, 441 U.S. at 777) and would frustrate the purposes of the statute by permitting those who wilfully engage in fraud in securities transactions to go unpunished.

2. Petitioner's remaining contentions are insubstantial and do not warrant review by this Court. Petitioner argues (Pet. 14-17) that the prosecutor concealed material exculpatory information by failing to disclose the criminal record of Raymond Starns, who had written the two uncashed and undeposited personal checks falsely listed as "cash on hand" in the financial statement given to the bank.

An IRS agent testified (Tr. 669) that petitioner admitted knowing that the checks were worthless. The agent also recalled that petitioner had stated that he realized that Starns had served time in jail for passing bad checks. Starns did not testify at petitioner's trial, but he did testify at the separate trial of petitioner's co-indictees. At that time, Starns

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[5] This is particularly true where, as here, the financial condition of the borrower is weak at the time the loan is made. The lender must depend to a substantial degree on the value of the pledged securities to insure repayment of the loan.

stated that, although he had been arrested for passing bad checks in 1963, he was not convicted on that charge (James App. 320).[6] Starns also testified that, in 1973, he was again arrested for passing a bad check (*id.* at 322) and was later convicted for uttering forged securities (James Tr. 1241-1243).[7]

Petitioner's claim that the prosecutor's failure to disclose Starns' criminal record violated the rule of *Brady* v. *Maryland*, 373 U.S. 83 (1963), was never raised in the district court. It was not, therefore, properly presented in the court of appeals, which did not discuss it. There is accordingly no necessity for this Court to consider the question. *United States* v. *Lovasco*, 431 U.S. 783, 788 n.7 (1977).

In any event, the claim is frivolous. Starns was not a witness for the government at petitioner's trial. His criminal record therefore could have no impeachment value. Nor could disclosure of the information have created a reasonable doubt regarding petitioner's guilt that would not otherwise exist. See *United States* v. *Agurs*, 427 U.S. 97, 102 (1976). To the contrary, the evidence of Starns' record would have confirmed that petitioner's treatment of Starns' uncashed checks as "cash on hand" was even more misleading than it appeared to be.

Finally, even if petitioner could have used the information about the chronology of Starns' arrests

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[6] "James App." refers to the joint appendix filed in the court of appeals in *United States* v. *Leonard James, et al.*, No. 78-1346 (2d Cir.).

[7] "James Tr." refers to the transcript of the trial of petitioner's co-indictees.

and conviction to show that he did not know the full extent of Starns' criminal record at the time when he prepared the false financial statement, that would not have tended to exculpate him.[8] Petitioner still knew that the checks listed as "cash on hand" were uncashed and undeposited personal checks (Tr. 668-669). They were not properly reported as "cash" items (Tr. 351-353). Moreover, petitioner was responsible for a host of other misrepresentations to the bank, as noted above. In this factual context, the details of Starns' criminal record could not have created a reasonable doubt as to petitioner's guilt. *United States* v. *Agurs*, *supra*, 427 U.S. at 113-114.

3. Petitioner also claims (Pet. 17-19) that the district court improperly admitted into evidence several pages of notes as prior consistent statements of an agent who testified on behalf of the government. This claim is refuted in the thorough opinion of the court of appeals, on which we rely.[9]

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[8] There is no substance to petitioner's suggestion that the prosecutor knowingly used perjured testimony. The government agent testified only that petitioner stated to him that petitioner was aware, when the financial statement was prepared, that Starns had been in jail for passing a bad check (Tr. 668-669, 782-787, 887-890). The agent did not purport to testify about Starns' record; he merely repeated his recollection of petitioner's words during their interview. When petitioner testified on his own behalf, he did not contradict the agent's testimony on this point. Petitioner's counsel had the opportunity to, and did, extensively cross-examine the agent about his recollection of petitioner's statement regarding Starns (Tr. 782-787).

[9] Petitioner appears to challenge the analysis in Judge Friendly's concurring opinion rather than that of the court's

Petitioner was interviewed on several occasions by government agents before the indictment was returned in this case. Several agents took notes during these interviews. Agent Thomas Cox, who testified at petitioner's trial, did not personally take notes, but he was present at the interviews, examined the notes, and testified that the notes accurately reflected what had been said (Tr. 875). Agent Cox used the notes to refresh his memory during his direct examination (Tr. 652-653). Petitioner's counsel used the notes extensively during his cross-examination of Agent Cox, and even read from them repeatedly before they were admitted into evidence (Tr. 762, 767-768, 784, 798, 800, 801, 807, 811, 816, 819, 820, 852, 864, 867, 872). The purpose of this cross-examination was to create the impression that Agent Cox's testimony differed from the notes. On redirect the government offered four excerpts from the notes to show that the agent's testimony was consistent with them (Tr. 882, 887, 890, 897).

Petitioner now claims that this evidence should not have been admitted because it did not satisfy the requirements of Fed. R. Evid. 801(d)(1)(B), as discussed in *United States* v. *Quinto*, 582 F.2d 224, 233-234 (2d Cir. 1978). These requirements are that the prior statement must be consistent with the witness' in-court testimony, must be offered to rebut an ex-

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opinion (Pet. 17-19). However, Judge Friendly fully agreed with the court's analysis of the prior consistent statement issue (Pet. App. 35a) and joined in the judgment affirming petitioner's conviction.

press or implied charge of recent fabrication, and must be made before a motive to fabricate arose.

As the court of appeals pointed out (Pet. App. 23a), no objection was made to the receipt of one of the exhibits and petitioner's counsel had already read the supposedly objectionable portion of another exhibit to the jury before the government offered it (Tr. 852, 882). Moreover, as the court of appeals also observed (Pet. App. 26a), inasmuch as petitioner had used portions of the notes to impeach Agent Cox and had read extensively from them, the government was entitled to place these passages in context by introducing additional portions of the notes under the doctrine of completeness. Fed. R. Evid. 106. When substantial portions of a prior statement are used in cross-examination of a witness, fairness dictates that additional relevant portions be admitted to avoid misleading the jury. *United States* v. *Lev*, 276 F.2d 605, 608 (2d Cir.), cert. denied, 363 U.S. 812 (1960).

Finally, even assuming that admission of the four excerpts was improper, any error was clearly harmless. As the court of appeals explained (Pet. App. 27a-29a), the notes were either entirely consistent with Agent Cox's detailed oral testimony or related to merely peripheral matters. There is no reason to assume that these "few pages of cryptic phrases" (Pet. App. 29a) had any appreciable effect on the jury, in view of the detailed testimony of the government agents regarding what petitioner said to them.

CONCLUSION

We do not oppose granting the petition for a writ of certiorari limited to the question whether a pledge of stock as collateral for a loan is an "offer or sale" within the meaning of the Securities Act of 1933 (Question One). In all other respects, the petition should be denied.

Respectfully submitted.

WADE H. MCCREE, JR.
Solicitor General

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WADE S. LIVINGSTON
Attorney

MARCH 1980

☆ U. S. GOVERNMENT PRINTING OFFICE: 1980 316518 268

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

No. 79-1013

WILLIAM RUBIN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR PETITIONER, WILLIAM RUBIN

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Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR PETITIONER, WILLIAM RUBIN

Question Presented

Whether a pledge of stock to a bank as collateral for a loan is a "sale" of a security under § 77q(a), Title 15, U.S.C. (Securities Act of 1933).

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Opinion Below

The opinion of the Court of Appeals is officially reported at 609 F.2d 51 (1979).

Jurisdiction

The Court of Appeals in a split decision affirmed the conviction. Timely petitions for rehearing and a suggestion for a hearing *en banc* were denied on November 20, 1979. By Order of the Court of Appeals previously issued on October 10, 1979, the Court of Appeals stayed the issuance of the mandate pursuant to Rule 41(a) of the Federal Rules of Appellate Procedure pending application to this Court for a writ of certiorari. The petition for a writ of certiorari was filed on December 19, 1979 and was granted on April 14, 1980. Jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

Statutory Provisions

§ 2(3), Securities Act of 1933, § 3(a)(13), (14), Securities Exchange Act of 1934, §§ 77q(a), 77x, Title 15, U.S.C., § 371, Title 18, U.S.C., have been set forth in the petition for the writ of certiorari at pages 3-4.

Title 15, United States Code

Sec. 79b(a)(23)

"'Sale' or 'sell' includes any sale, disposition by lease, exchange or pledge, or other disposition."

Title 18, United States Code

Sec. 1014

"Whoever knowingly makes any false statement or report, . . . for the purpose of influencing in any

way the action of . . . any bank the deposits of which are insured by the Federal Deposit Insurance Corporation, . . . upon any application, advance, discount, purchase, purchase agreement, repurchase agreement, commitment, or loan, or any change or extension of any of the same, by renewal, deferment of action or otherwise, or the acceptance, release, or substitution of security therefor, shall be fined not more than $5,000 or imprisoned not more than two years, or both."

Securities Exchange Act of 1934

Sec. 10(b)

"To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Code of Federal Regulations, Vol. 17, § 240.10b-5

Rule 10b-5

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

"(a) To employ any device, scheme, or artifice to defraud,

"(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

"(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

"in connection with the purchase or sale of any security."

Statement of the Case

Petitioner was indicted on January 27, 1978 in three counts. Count 1 charged a conspiracy under Section 371 of Title 18, U.S.C., to violate (a) Section 17(a) of the Securities Act of 1933 (77q(a) and 77x of Title 15, U.S.C.), (b) Section 77e of Title 15, U.S.C., (c) Sections 1014 and 2 of Title 18, U.S.C., and (d) Sections 1341 and 1343 of Title 18, U.S.C. Counts 2 and 3 charged violations of Sections 1014 and 2 of Title 18, U.S.C., and violations of Sections 77q(a) and 77x of Title 15, U.S.C., respectively.

The part of the conspiracy which is at issue here is that which charged a violation of Sections (17(a), 77q(a) and 77x, Title 15, U.S.C.). As part of the objects and means whereby that part of the conspiracy was committed, the indictment charged that the fraud in obtaining loans from the Bankers Trust Company occurred by pledging as collateral to said bank common stock of All-State Insurance Company, Satellite Systems Corp., General Investment Corp. and Marlin International Company.

Rubin is 48 years old, having been born in New York. He graduated from New York University in 1951. He at-

tended the New York Law School at night and graduated in 1960. Rubin was neither admitted to the Bar nor did he practice law. In 1956 he became a CPA. Rubin formed his own accounting firm in 1975 and has conducted it since then as a senior partner of W. R. Rubin & Co. (R.* 1638-1639). Between 1961 and 1970 Rubin was with the accounting firm of Fred Landau & Co. (R. 1776). He left Landau & Co. and the accounting business in 1970 to form his own firm specializing in mergers and acquisitions (R. 1777, 1781-1782). In September or October, 1971, he accepted employment with North American Planning Corp., a public brokerage company in which he was a business consultant and a member of the board of directors (R. 1787).

When North American began to have financial difficulty, he sought additional financial help from others which led him to co-defendant Leonard James, who was a former Internal Revenue agent and who Rubin knew had been previously employed by Dugan's Bakery, a former client of Landau & Company (R. 1798). Through James some financial help was obtained (R. 1799) as well as an introduction to co-defendant Deaton with whom James was then in the coal and energy business as Tri-State Energy Company (R. 1803). To Rubin, Deaton alleged himself to be an expert on coal and gas, a forecaster of the shortage of energy, a man who had apparently been in the pipeline business for many years, and a bright, articulate, and charming individual (R. 1803-1804).

When North American was taken over by a trustee in August or September of 1972 on application of the SEC, Rubin left the company to go with Tri-State Energy.

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* The letter "R" followed by a number designates page references to the trial transcript.

Deaton and James had told Rubin that Tri-State's prospects were tremendous and the profits dealing in coal and gas substantial (R. 1836-1837). While he was told Tri-State had a cash flow problem, he was further told discussions with others were being had which would bring in millions to Tri-State (R. 1837-1838). Although Rubin was told he would make money with them, Deaton refused to give him a stock interest in the business which was owned, he said, 50-50 by James and him (JA178*; R. 1838). Rubin agreed to go with the company and as compensation to receive $2,000 a month, a $10,000 Christmas bonus (R. 1837), and 20% of the profits (R. 1838, 1841).

Because Tri-State needed capital Rubin approached the Bankers Trust Company with whom he had had excellent relations while with Landau & Co. and with whom he had negotiated loans in behalf of clients of Landau. Rubin had met Raymond Ludwig of that bank and sought from him on October 19, 1972 for Tri-State a $5,000,000 loan which the company needed to operate the mine (R. 1855). Ludwig declined the loan of that size (R. 1855). Instead Ludwig said:

> "I am going to put you on for $50,000 for 30 days. At the end of the 30 days, if you can produce an up-to-date financial, we . . . will see your track record." (R. 1859)

Ludwig introduced petitioner and Deaton to his assistant John Keating on that day. Keating was a prosecution witness. He was told the bank was making a loan to Tri-State Energy which was in the coal business with mines in Kentucky and which needed the loan for payroll at the mine (JA6; R. 222, 224). Keating was further instructed

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* The letters "JA" followed by a number designates page reference to the joint appendix.

by Ludwig to open checking accounts and process the loan as he would do normally with any new account (R. 222). The documents obtained were the execution of a promissory note for $50,000 (JA6-7, 122), a Tri-State corporate resolution authorizing the execution of the promissory note, the opening of a bank account, the execution of the signature cards, the right to borrow money, and the individual guarantees of the loan by Rubin and co-defendants Deaton and James (JA6-7; R. 227). None of the documents executed by the borrower on that day or any subsequent day specifically dealt with collateralizing the loan. Keating said Ludwig told him on October 19, 1972 that "we would be receiving collateral on the loan" (JA8). A certificate for 400,000 shares of American Leisure Corporation common stock bearing a legend that the stock was restricted was received at the bank from the borrower on October 20, 1972 (*id*). A financial statement of the borrower containing a balance sheet dated October 20, 1972 (JA39-40; GX 49, B-2c) was subsequently given to Keating on October 27, 1972 (JA40-41). The statement reflected the borrower's net worth as $7,100,000. Besides the financial statement the bank received in late October or early November, 1972 a written three month projection of the borrower's prospective income (JA40-41; GX 49, A-19). The projection plotted gross income of $540,000 based on purported spot sales of coal to Continental Coal Corporation and Repoca Resources, as well as a long term contract with Roland Werkstatten, a German company (JA42). The bank considered this projection the single most "significant document" it received from the borrower because it was from this information that the bank could determine how the loan repayments were to be made:

> "A. [Keating] Document A-19 is a projection that was prepared by Mr. Rubin and delivered to me by Mr. Rubin.
>
> * * *

Q. About when did he deliver it to you?

A. It was sometime after the initial loan was made, October, late October, early November 1972.

Q. Did you have any discussions with him concerning it?

A. Yes. This was the—as far as I was concerned, this was one of the most important documents that I had received from the company. What it did is it gave me an analysis of when the company was going to generate cash from the sale of coal and how much was going to be generated and when the—what the cash would be used for and what the net figure or net cash flow of the company was so that that could be used to retire any bank loans that had been made.

Now, the document indicates that sales would be made of $120,000 in December 1972, 240 in January of 1973, and 180 in February of 1973.

Now, the sales that are associated with this were $300,000 from a Continental Coal Corporation and $240,000 from Repoca Resources." (JA42)

An additional three months loan of $50,000 was made on November 20, 1972 (JA15, 128). The original one month loan of $50,000 was extended for three months on November 22, 1972 (JA16, 130). A further loan of $100,000 was made on November 30, 1972 (JA18, 132) and on December 6, 1972 a further loan was made of $275,000 (JA20, 134). The total lent was the sum of $475,000. Additional collateral was received by the bank after October 20, 1972. 2,000 shares of All-State Life Insurance Company was received by the bank on November 10, 1972 (JA66, 168). 100,000 shares of Management Dynamics, Inc. was received December 6, 1972, but was returned by the bank to the borrower for 175,000 shares of General

Investment stock and received by the bank on December 19, 1972, 50,000 shares of stock of Satellite Systems Corporation was received on January 19, 1973, and 20,000 shares of Marlin Investment stock was received on January 30, 1973 (JA66, 168). The additional loans by the bank between November 20 and December 6 were made after the borrower's three month gross income projection was received by the bank, said Keating, and it was that projection which was "taken into account in making these further loans" (JA71).

In describing the nature of these loans Keating referred to a bank record, that is, an "offering ticket" (JA9) which reflected interest on the loan, the type of loan, and a notation "lien stock 400,000 shares American Leisure Corp." which he said was given as collateral for the loan (JA10). Lien stock, Keating stated, is in bank jargon "side collateral". "Side collateral" was defined in the following colloquy between Keating and the prosecutor

> "Q. Now, when you said 'side collateral,' can you tell us what you mean by that?
>
> A. Well, when the loan was made initially, the loan was envisioned that it would be repaid from the ongoing operations of the corporation, namely from the sale of coal or natural gas. The collateral was taken as a secondary source of repayment in the event that the primary source, the ongoing operations of the corporation didn't materialize." (JA10-11)

On February 26, 1973 despite the fact that the loans totalling $475,000 had matured and had not been paid, the bank, believing the loans would nevertheless be paid, requested the borrower to execute a demand note for

$475,000 covering the previous loans made between October 20 and December 6 (JA58, 139). Although the stock collateral was still held by the bank the demand note executed by the borrower, said Keating, was "a yellow form associated with an unsecured loan, although this particular loan was not. The reason that that note was utilized rather than a secured note form was because we believed the primary source of repayment was going to come from the operations of the coal mine and the gas fields and the collateral that was taken at that time was in what we call side collateral or lien collateral, and that was basically under a security agreement which was given to us in connection with the loans." (JA67).

Two days later after receiving an inquiry from the Justice Department about the borrower (JA59-60), the bank on March 5, 1973 demanded payment of the loan (JA60). The loan was not paid. The bank did not foreclose or attempt to sell the collateral. Instead it instituted a suit in the Supreme Court, County and State of New York (JA88, 175). Petitioner signed a confession of judgment for over half a million dollars with interest and attorneys fees added (JA120, 175).

Summary of Argument

To construe the definitional terms of "sale" and "purchase" in the anti-fraud provisions of the Securities Acts of 1933 and 1934 as including a pledge of stock as collateral for a commercial loan "would add a gloss to the operative language of the statute quite different from its commonly accepted meaning", as this Court noted in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 185, 199, 96 S.Ct.

1375, 1383 (1976). "Sale" and "purchase" are ordinary, commonly understood words which involve a transfer of title or ownership from one person to another. A pledge as collateral for a loan is a deposit of personal property as security with an implied or express power of sale upon default. The legislative history of the anti-trust provisions of the Securities Acts of 1933 and 1934 defining "sale" and "purchase" reveals no trace of any Congressional intent to regulate transactions involving a pledge of securities. As this Court has often stated:

> "When Congress wished to provide a remedy to those who neither purchased nor sold securities it had little trouble in doing so expressly." *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 734, 95 S.Ct. 1917, 1925 (1975).

Because one of the remedial purposes of the Securities Acts was to protect investors from the type of fraudulent conduct that may have existed in the instant case does not justify extending the scope of the anti-fraud provisions of the Securities Acts beyond Congressional intent and beyond the common meaning of the terms "sale" and "purchase". This Court as late as the end of this Term said in *Aaron* v. *SEC,* No. 79-66, 48 U.S.L.W. 4609, 4613 (decided June 2, 1980):

> "Though cognizant that 'Congress intended securities legislation enacted for the purpose of avoiding frauds to be construed "not technically and restrictively, but flexibly to effectuate its remedial purposes,"' *Affiliated Ute Citizens* v. *United States, supra,* at 151, quoting, *SEC* v. *Capital Gains Research Bureau, supra,* at 195, the Court has also noted that 'generalized references to the "remedial purposes"' of the securities laws 'will not justify

> reading a provision "more broadly than its language and statutory scheme reasonably permit."' *Touche Ross & Co.* v. *Redington,* 442 U.S. 560, 578, quoting, *SEC* v. *Sloan,* 436 U.S. 103, 116. Thus, if the language of a provision of the securities laws is sufficiently clear in its context and not at odds with the legislative history, it is unnecessary 'to examine the additional considerations of "policy" . . . that may have influenced the lawmakers in their formulation of the statute.' *Ernst & Ernst* v. *Hochfelder, supra,* at 214, n. 33."

The interests and liabilities created by pledge transactions involving ordinary commercial loans are regulated by state law. Adequate remedy exists under said laws to protect those interests without burdening the federal courts with unnecessary and unwarranted criminal or civil actions. *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. *supra* at 741.

For these reasons the decisions of the Fifth and Seventh Circuits in *National Bank of Commerce of Dallas* v. *All American Assurance Company, et al.,* 583 F.2d 1295, 1298 (5th Cir. 1978), and *Lincoln National Bank* v. *Herber,* 604 F.2d 1038, 1040 (7th Cir. 1979), that a mere pledge of stock for an ordinary commercial loan is not a "sale" or "purchase" within the anti-fraud provisions of the 1933 and 1934 Acts are a proper reflection of this Court's opinions and the Congressional intention. The opinions of the Courts of Appeals for the Second and Sixth Circuits in *United States* v. *Gentile,* 530 F.2d 461 (2d Cir. 1976), cert. den., 426 U.S. 936 (1976), *Mallis* v. *Federal Deposit Insurance Corp.,* 568 F.2d 824 (2d Cir. 1977) cert. granted, 431 U.S. 928, 97 S.Ct. 2630, 53 L.Ed.2d 243, cert. dismissed, *sub nom Bankers Trust Co.* v. *Mallis,* 435 U.S. 381, 98 S.Ct. 1117, 55 L.Ed.2d 357 (1978), and *Mans-*

bach v. *Prescott, Ball & Turben,* 598 F.2d 1017 (6th Cir. 1979), which are to the contrary, should not be supported.

For these reasons the judgment of the Court of Appeals should be reversed.

POINT I

The pledge of securities as collateral for a loan is neither a "sale" nor a "purchase" for the purpose of invoking the anti-fraud provisions of the Securities Acts.

The Court of Appeals below held without addressing the issue before this Court that

> "We have examined each of the other points raised by Rubin and find them to be without merit." 609 F.2d supra, at 66

Presumably that conclusion was based upon the Court of Appeals prior decision in *United States* v. *Gentile,* 530 F.2d 461 (2d Cir. 1976), cert. den., 426 U.S. 936 (1976), a decision relied upon by the District Court in its holding that a pledge of securities by Tri-State Energy, Inc. for the loan from the Bankers Trust Company was as a matter of law a "sale" within the meaning of § 77q(a), Title 15, U.S.C. (R. 2669). *Gentile* was a decision urged by the prosecutor as having "plainly reached the correct result . . .", and, the prosecutor added, was equally supported by the Court of Appeals decision in *Mallis* (Gov't brief in the Court of Appeals, pp. 79-80).

In *Gentile,* the Court of Appeals held that a pledge was within the literal definition of a "sale" under § 2(3), 15 U.S.C. § 77(b)(3) of the Securities Act of 1933, and that there is no requirement that title pass to con-

stitute a "sale" within the meaning of the statute. 530 F.2d *supra* at 466. In *Mallis,* a civil action for fraud under Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934, the Court of Appeals held:

> "We believe that the rationale underlying our holding in *Gentile* with respect to Sections 2(3) and 17(a) of the 1933 Act is persuasive authority for holding that a pledge constitutes a 'contract to sell or otherwise dispose of' a security within the meaning of Section 3(14) of the 1934 Act. Accordingly, on the facts of this case, we hold that both a 'sale' and a 'purchase' may be cognizable under Section 10(b) of the 1934 Act. Appellants were purchasers by virtue of their acceptance of the pledge by Arnold and Fowler; and Bankers Trust was a seller by virtue of its release of the Kateses' pledge." 568 F.2d *supra* at 820.

Gentile expressly rejected the Court of Appeals' decision in *McClure* v. *First National Bank,* 497 F.2d 490 (5th Cir. 1974), cert. den. 420 U.S. 930 (1975) which had held:

> "[M]ere acceptance of a stock pledge as collateral in a privately negotiated transaction between borrower and lender does not, of itself, bring within the scope of the federal securities acts a transaction otherwise outside their purview."

The term "sale" is defined in the Securities Act of 1933, ¶ 2(3), 15 U.S.C. § 77b(3), to include "every contract of sale or disposition of a security or interest in a security, for value." The 1934 Act defines a "sale" to include "any contract to sell or otherwise dispose of", and defines the words "buy" or "purchase" to include "any contract to buy, purchase, or otherwise acquire." §§ 3(a)(13) and (14),

15 USC § 78c(13) and (14). While the issue in this case involves a charge of conspiracy to violate, among other objects, § 77q(a), Title 15, U.S.C. (1933 Act) in committing a fraud in the "sale" of a security, it does not appear that Congress in enacting a similar anti-fraud provision under the 1934 Securities Act intended to alter the 1933 Act definition of "sale" even though there does exist a slight difference in wording. As the Court of Appeals noted in *National Bank of Commerce of Dallas* v. *All American Assurance Company, et al.,* 583 F.2d 1295, 1298 (5th Cir. 1978):

> "Although there are slight differences in wording between the 1933 Securities Act and the 1934 Securities Exchange Act, the definitions of these terms are functionally equivalent and are for the purposes of this case so treated. [Cases cited]."

Neither the Securities and Exchange Commission nor the other courts of appeals who are in conflict on whether a pledge is a "sale" or a "purchase" under the anti-fraud provisions of the Securities Acts of 1933 or 1934 take issue with that conclusion of the Court of Appeals in *National Bank of Commerce of Dallas* v. *All American Assurance Company, supra.* See, for example, brief of the Commission, amicus curiae, on the merits (pp. 12-13) submitted in *Bankers Trust Company* v. *Mallis,* 431 U.S. 928, 97 S.Ct. 2630, 53 L.Ed.2d 243, dismissed 435 U.S. 381, 98 S.Ct. 1117, 55 L.Ed.2d 357 (1978). We believe this proposition has further support in the fact that the 1933 and 1934 Acts were passed by the same Congress and should be considered together as this Court noted in *Tscherepnin* v. *Knight,* 389 U.S. 332, 342, 88 S.Ct. 548, 19 L.Ed.2d 564 (1967).

We further submit that the holdings in *Gentile* and *Mallis,* and later in *Mansbach* v. *Prescott, Ball & Turben,*

incorrectly construe the definitions of "sale" and "purchase" in the 1933 and 1934 Acts to include a pledge of stock as collateral for a loan.

The legislative history of the provisions defining "sale" and "purchase" reveals no trace of any Congressional intent to regulate transactions involving a pledge of securities as collateral for a commercial loan from a bank. As this Court stated in *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. 723, 734, 95 S.Ct. 1917, 1925, 44 L.Ed.2d 539:

> "When Congress wished to provide a remedy to those who neither purchased nor sold securities, it had little trouble in doing so expressly."

Congress could obviously have said so, as it did in the Public Utility Holding Company Act of 1935. There Congress provided that " 'sale' or 'sell' includes any sale, disposition by lease, exchange or pledge, or other disposition." § 79b(a)(23), Title 15, U.S.C. That Act like the Securities Acts of 1933 and 1934 contained anti-fraud provisions. § 79*l*(d), Title 15, U.S.C.

The meaning of the words "sale" and "purchase" under the Securities Acts of 1933 and 1934 held in *Gentile* and *Mallis* to include a pledge of stock as collateral for a commercial loan, we submit, "would add a gloss to the operative language of the statute quite different from its commonly accepted meaning." *Ernst & Ernst* v. *Hochfelder, supra.* In *Blue Chip Stamps* v. *Manor Drug Stores, supra,* this Court also stated that an act of Congress which defines a word of long usage should be interpreted to have intended its "long established legal meaning" in the absence of "unmistakeable support in the history and structure of the legislation." 421 U.S. *supra* at 756, 95 S.Ct. *supra* at 1917 (Con. Op. of Mr. Justice Powell). "Sale"

and "purchase" are well-defined words of legal and commonly accepted meaning.

SALE: "Contract whereby the absolute, or general, ownership of property is transferred from one person to another for a price, or sum of money, or, loosely, for any consideration." Webster's Third New International Dictionary (1964).

PURCHASE: (1) . . . (2) ACQUISITION . . .; the acquiring of title to or property in anything for a price: a buying for money or its equivalent (the number of shares in a business)." Webster's Third New International Dictionary (1964).

PLEDGE: 1. . . . b: a chattel or object of personal property delivered by a debtor or obligor to a creditor or obligee to be kept by the latter until the debt or obligation is satisfied: an object given as security by pledge c (1) a bailment or a chattel or object of personal property as security for the satisfaction of a debt or other obligation . . ." Webster's Third New International Dictionary (1964).

"Sale" and "purchase" in both common and ordinary understanding mean the acquisition and disposition of ownership.

> "At common law a pledge would be readily distinguishable from a sale since a pledge involves a transfer of possession only, not of title." *Lincoln National Bank* v. *Herber,* 604 F.2d 1038, 1040 (7th Cir. 1979).

See, *Pauly* v. *State Loan & Trust Co.*, 165 U.S. 606, 17 S.Ct. 465 (1897) (State Loan & Trust Co. pledgee of stock of California Nat'l Bank held as collateral for a loan, is not an owner of the pldeged stock liable under a federal statute holding a shareholder of California Nat'l Bank responsible for its debts).

It is equally well-established that a pledge of stock as collateral for a loan is not a "sale" or "purchase". Ownership rights remain with the pledgor while the interest the pledgee obtains is merely the security interest that entitles the pledgee to sell the stock on default. To characterize the pledgor as a "seller" and the pledgee as a "purchaser" of the pledged security is, we submit, to pervert the ordinary and commonly understood relationship between the two. A pledge is a "deposit of personal property as security with an implied power of sale upon default." L. Jones, Collateral Securities and Pledges, § 1 (3d ed. 1912); Restatement of Security, § 1 (1941)

> "One does not normally speak of the 'purchase' or 'sale' of a loan . . ." *SEC* v. *Fifth Ave. Coach Lines,* 289 F.Supp. 3, 38 (S.D.N.Y. 1970), aff'd, 435 F.2d 510 (2d Cir. 1970).

The differences between these terms were appropriately described in *National Bank of Commerce of Dallas* v. *All American Assurance Company, supra*:

> "The rights and privileges of the parties are not affected by a pledge in the same manner as by a 'sale' or 'purchase.' The pledgor generally (1) has the right to sell the stock subject to the security interest, (a) is entitled to vote the stock, (3) has the right to receive all dividends, and (4) continues to be liable for ad valorem taxes.

See generally, L. Jones, Collateral Securities and Pledges §§ 1, 176a, 441, 602 (3d ed. 1912).

"The pledgee, on the other hand, has 'no general property right in the thing pledged, but only a right upon default, to sell in satisfaction of the pledgor's obligation.' *Pauly* v. *State Loan & Trust Co.,* 165 U.S. 606, 622, 17 S.Ct. 465, 471, 41 L.Ed. 844 (1897). The pledgee does not participate in any appreciation of the stock, has none of the rights normally accorded shareholders, and has no right to sell the collateral for its own account. Indeed, its relationship is of a fiduciary character, *Easton* v. *German-American Bank,* 127 U.S. 532, 437, 8 S.Ct. 1297, 32 L.Ed. 210 (1888), and it must account for all proceeds in excess of the debt and profits accruing as a result of possession of the collateral. Restatement of Security ¶ 27 (1941)." (583 F.2d *supra* at 1300).

Both Courts of Appeals in *National Bank of Commerce of Dallas* v. *All American Assurance Company, supra,* and *Lincoln National Bank* v. *Herber, supra,* recognized that the statutory definition of "sale" which under the 1933 Act includes "every . . . disposition of a security or interest in a security, for value" and the or "otherwise dispose" or "otherwise acquire" of the language of the 1934 Act was broad enough to include a pledge transaction. However, both Courts of Appeals, correctly we submit, rejected such a "literal approach" to the definitions in the Acts as was done in *Gentile* and *Mallis* because such a "literal approach" was contrary to the ordinary and common understanding of a pledge of stock given as collateral for a loan. Both Courts of Appeals adopted and followed the reasoning of this Court in rejecting a "literal" application of the securi-

ties laws in favor of an analysis looking to underlying economic realities. See *United Housing Foundation, Inc.* v. *Forman,* 421 U.S. 837, 849, 95 S.Ct. 2051, 44 L.Ed.2d 621 (1975) ("Because securities transactions are economic in character Congress intended the application of these statutes to turn on the economic realities underlying a transaction . . ."); *Tscherepnin* v. *Knight,* 389 U.S. 332, 88 S.Ct. 548, 553 (1967) ("[I]n searching for the meaning and scope of the word 'security' in the Act[s], form should be disregarded for substance and the emphasis should be on economic reality.").

Bankers Trust Company lent $450,000 to Tri-State upon promissory notes collateralized by a pledge of stock certificates at the time the loans were issued. There can be no suggestion that the form of this transaction between Bankers Trust Company and Tri-State Energy, Inc. did not represent the substance of the matter. Indeed, the "reality" of the instant transaction is that the Bankers Trust Company simply lent money to Tri-State Energy primarily because of its belief in the solvency of that company and the ability of that company to generate sufficient income to repay the loan on maturity. The pledge of the stock as collateral was merely a secondary source for the bank in the event there was a default of the loan. This is abundantly clear from the testimony of Keating from the Bankers Trust Company who said:

> "[W]hen the loan was made initially, the loan was envisioned that it would be repaid from the ongoing operations of the corporation, namely from the sale of coal or natural gas. The collateral was taken as a secondary source of repayment in the event that the primary source, the ongoing operations of the corporation didn't materialize." (JA10-11).

In sum, the pledge of stock as security for the loan with the Bankers Trust Company was in fact and common usage a garden variety pledge and not a "sale" or "purchase". Common accepted meaning and long-established legal definition, as well as established canons of statutory construction, support the correctness of the views of the Courts of Appeals in *National Bank of Commerce of Dallas* and *Lincoln National Bank* that a mere pledge of stock as security for a loan is not within the definitions of "sale" or "purchase" under the 1933 and 1934 Securities Acts.

POINT II

Sound policy reasons indicate that Congress never intended to extend the anti-fraud provisions to pledge transactions.

This Court has frequently had occasion to note that the fundamental purpose of the Securities Acts was to protect investors against false and deceptive practices that might injure them. *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 151, 92 S.Ct. 1456, 1470, 31 L.Ed.2d 741, 760 (1972); *Superintendent of Insurance* v. *Bankers Life & Casualty Co.,* 404 U.S. 6, 11-12, 92 S.Ct. 165, 168, 30 L.Ed.2d 128, 134 (1971); *J. I. Case Co.* v. *Borak,* 377 U.S. 426, 432-433, 84 S.Ct. 1555, 1559-1560, 12 L.Ed.2d 423, 427-428 (1964). Bankers Trust Company by virtue of its acceptance of the pledge of certificates of stock from Tri-State Energy neither made an investment in the pledged securities nor did the bank by its mere acceptance of the pledge affect the securities industry as suggested in *Gentile.* Bankers Trust Company looked to the pledged collateral as a "secondary source of repay-

ment in the event that the primary source, the ongoing operations of the corporation, did not materialize." (JA10-11). Bankers Trust Company did not accept the pledged stock for distribution or for any other purpose except the traditional purpose of securing the loan.

As Professor Loss has stated:

> "Federal legislation was hardly needed for privately negotiated pledge transactions between borrowers and lenders." (L. Loss, Securities Reg. 649 (2d ed. 1961)).

Gentile, we submit, expanded the meaning of "sale" beyond what Congress intended and what was necessary to effect the remedial purposes of the 1933 Act. *Mallis,* we submit, did the same thing with respect to Section 10(b) of the 1934 Act. As the Court of Appeals noted in *National Bank of Commerce of Dallas, Gentile* predicated its holding upon its statement:

> "The pledgee takes a legally enforceable interest in the pledged securities which he assumes will compensate for any default on the underlying loan. The pledgee thereby decreases the risk that he will suffer loss due to nonpayment of the loan. In effect, the pledgee assumes a very real investment risk that the pledged securities will have continuing value, a risk that is identical in nature to the risk taken by investors which serves as the indisputable basis for statutory regulation of securities transactions." (530 F.2d *supra* at 467).

The Court of Appeals in *National Bank of Commerce of Dallas* correctly responded that:

> "This rationale might be a persuasive argument that the federal securities laws ought to encom-

> pass pledges, as well as purchases and sales. It does little to support a decision that they in fact do cover pledges. Congress can be presumed to know the difference between a collateral pledge transaction and a sale and purchase. If it had intended to cover both, it could have easily done so by words traditionally used to differentiate between the two." (583 F.2d *supra* at 1300).

Further criticism of this statement in *Gentile* was noted in *Lincoln National Bank* v. *Herber,* 604 F.2d *supra* at 1043:

> "[W]e disagree with this analysis. Risk there is, but the risk is not an *investment* risk. It is the ordinary *commercial* risk taken by any secured lender. The risk that the pledgor does not own the collateral he purports to own exists no matter what the nature of the collateral."

Bankers Trust Company did not make an investment in Tri-State stock. The bank did not accept the collateral for profit it might make on the stock pledged at the time the loans were made as it would if it was an investor. Cf. *United Housing Foundation* v. *Forman,* 421 U.S. *supra* at 851:

> "Common sense suggests that people who intend to acquire only a residential apartment in a state-subsidized cooperative, for their personal use, are not likely to believe that in reality they are purchasing investment securities simply because the transaction is evidenced by something called a share of stock. * * * In short, the inducement to purchase was solely to acquire subsidized low-cost living space; it was not to invest for profit."

Similarly, the acceptance by the Bank of the pledged collateral was to secure the loan in the event of default; "it was not to invest for profit."

"A commercial bank's business is lending money, not trading in securities." *McClure* v. *First National Bank,* 497 F.2d *supra* at 495.

The absence of any Congressional intent to include a pledge transaction as a "sale" or "purchase" in the 1933 and 1934 Acts is further reflected in the fact that before the decision in *SEC* v. *Guild Films Co.,* 279 F.2d 485 (2d Cir. 1960), cert. den. 364 U.S. 819 (1960), on which the holdings in *Gentile* and *Mallis* are based, or at least shortly before the SEC's submission in *Guild Films,* the SEC did not publicly contend that a pledge of stock as collateral for a commercial loan was a "sale" or a "purchase" under the 1933 and 1934 Securities Acts (L. Loss, Securities Reg. 645 (2d ed. 1961)). The uncertain scope of the decision in *Guild Films* was so severely questioned that Judges in the District Court in the Southern District of New York declined to apply federal jurisdiction to such pledge transactions under the anti-fraud provisions of the Securities Acts. *Fox* v. *Glickman Corp.,* 253 F.Supp. 1005, 1011-1012 (S.D.N.Y. 1966); *Investment Properties Intl. Ltd.* v. *I.O.S. Ltd.* [1970-1971], F.Sec.L.Rep. (CCH) par. 93,011 (S.D.N.Y. 1971). Indeed, at the time of the instant loans from Bankers Trust Company in 1972, Rubin's conduct, even assuming it was fraudulent for purposes of this appeal, was not considered violative of Section 77q(a), Title 15, U.S.C., or Section 10(b) of the 1934 Act, criminally or civilly, because a pledge of stock as collateral for a loan had been held in the Southern District of New York not to be a "sale" or a "purchase" under the Securities Acts.

What *Gentile* suggests, we submit, is that the fraud in that case in which the banks made loans on pledged embezzled stock certificates warranted an extension of the statutory definitions of "sale" and "purchase" to embrace a pledged transaction. Merely because one of the remedial purposes of the Securities Acts was to protect investors from such type of fraudulent behavior as in *Gentile,* or as may have existed in the instant case, does not mean that the anti-fraud provisions should be stretched beyond what Congress intended and contrary to the common meaning of the words "sale" and "purchase" in order to cover such type of conduct. Indeed, in *Aaron* v. *SEC, supra,* this Court recently stated:

> "Though cognizant that 'Congress intended securities legislation enacted for the purpose of avoiding frauds to be construed "not technically and restrictively, but flexibly to effectuate its remedial purposes,"' *Affiliated Ute Citizens* v. *United States, supra,* at 151, quoting, *SEC* v. *Capital Gains Research Bureau, supra,* at 195, the Court has also noted that 'generalized references to the "remedial purposes"' of the securities laws 'will not justify reading a provision "more broadly than its language and statutory scheme reasonably permit."' *Touche Ross & Co.* v. *Redington,* 442 U.S. 560, 578, quoting, *SEC* v. *Sloan,* 436 U.S. 103, 116." (48 U.S.L.W. *supra* at 4613)

Simply put, fraudulent representations as to the nature and value of the securities pledged for ordinary commercial loans are neither within Section 77q(a) of Title 15 U.S.C. (1933 Act) nor within Section 10(b) of the 1934 Act since a pledge of stock does not constitute a "sale" or a "purchase" of a security within the meaning of those statutes. When Congress needed to impose special defini-

tions upon common words in order to effectuate the remedial purposes of an act it had little trouble doing so. *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. *supra* at 734, 95 S.Ct. *supra* at 1925; *Public Utility Holding Company Act of 1935;* Section 79b(a)(23), Title 15, U.S.C.

There was, we submit, no need for Congress to extend Section 77q(a) of Title 15, U.S.C. (1933 Act) or Section 10(b) of Title 15, U.S.C. (1934 Act) to pledges in order to effectuate its anti-fraud purposes.* The parties to a pledge transaction are situated quite differently from purchasers and sellers of securities in terms of legal recourse under state law. The pledgee, unlike a securities purchaser, has a remedy on a promissory note against the maker and any guarantor. *National Bank of Commerce of Dallas* v. *All American Assurance Company,* 583 F.2d 1295, 1300 (5th Cir. 1978). Indeed, that is exactly what Bankers Trust Company did in the instant case. It sued the borrower and the guarantors on the promissory notes in the Supreme Court, County and State of New York, and obtained a confession of judgment from the petitioner (JA88, 175).

The Court of Appeals in *Lincoln National Bank* v. *Herber, supra,* appropriately stated:

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* Significantly, the securities fraud which was charged as an object of the conspiracy under § 77q(a), Title 15, U.S.C., together with the violation of § 1014, Title 18, U.S.C., was unnecessary since the fraudulent representation as to the pledged collateral was also considered by the prosecutor as part of the violation under § 1014. The prosecutor so advised the District Court as follows:

> "Ms. Neugarten: Count 2 subsumes all false statements as to collateral, not just Marlin but the five other securities, since 1014 specifically includes false statements as to collateral and substitution of collateral." (R. 2309)

> "The final consideration counselling against extension of the antifraud provisions of the 1933 and 1934 Acts to the situation where securities are fraudulently pledged as collateral for a bank loan is that state law already extensively occupies the field. This would be a further indication that Congress never intended to extend the antifraud provisions to pledge transactions as well as a sound policy reason not to extend the federal securities laws into this area, as there is no apparent need." (604 F.2d *supra* at 1044).

And further,

> "State regulation of a field and the availability of remedies under state law have both been considered by the Supreme Court in a number of recent decisions declining to imply a private right of action under various sections of the securities laws. *See, e.g., Santa Fe Industries, Inc.* v. *Green,* 430 U.S. 462, 97 S.Ct. 1292, 51 L.Ed.2d 480 (1977); *Piper* v. *Chris-Craft Industries, Inc.,* 430 U.S. 1, 97 S.Ct. 926, 51 L.Ed.2d 124 (1977); *Cort* v. *Ash,* 422 U.S. 66, 95 S.Ct. 2080, 45 L.Ed.2d 26 (1975)." (604 F.2d *supra* at 1044).

Relegating such conduct involved in a pledge transaction to the state courts is where such transactions belong since such security interests are adequately regulated by state laws. The inevitable consequences of extending the scope of Sections 77q(a) and 10(b) to pledge transactions would be to increase litigation in the federal courts without any increased protection to the parties. See *Blue Chip Stamps* v. *Manor Drug Stores,* 421 U.S. *supra* at 741.

CONCLUSION

The judgment of the Court of Appeals should be reversed.

Respectfully submitted,

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Supreme Court, U. S.
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No. 79-1013

In the Supreme Court of the United States

OCTOBER TERM, 1979

WILLIAM RUBIN, PETITIONER

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UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

QUESTION PRESENTED

Whether the pledge of stock by petitioner and his co-conspirators as collateral for a loan was an "offer" or "sale" of securities (terms defined by statute to include every disposition or attempt to dispose of an interest in a security for value) and thus was subject to the antifraud provisions of Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a).

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OPINION BELOW

The opinion of the court of appeals (Pet. App. 1a–67a) is reported at 609 F.2d 51.

JURISDICTION

The judgment of the court of appeals was entered on September 6, 1979. A petition for rehearing was denied on November 20, 1979. The petition for a writ of certiorari was filed on December 19, 1979, and was granted on April 14, 1980. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTES INVOLVED

Section 2(3) of the Securities Act of 1933, 15 U.S.C. 77b(3), provides in pertinent part:

> The term "sale" or "sell" shall include every contract of sale or disposition of a security or interest in a security, for value. The term * * * "offer" shall include every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value.

Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), provides:

> It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—
>
> (1) to employ any device, scheme, or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light

of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

STATEMENT

1. Following a jury trial in the United States District Court for the Southern District of New York, petitioner was convicted on one count of conspiring to violate various federal antifraud statutes, including Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), in violation of 18 U.S.C. 371.[1] Petitioner was sentenced to three years' imprisonment. The court of appeals affirmed (Pet. App. 1a–67a).[2]

The evidence at trial showed that in 1972, following the collapse of the stock brokerage firm in which petitioner was a principal (Tr. 1820), petitioner became vice-president of Tri-State Energy, Inc. ("Tri-State") (Tr. 228,

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[1] The conspiracy count of the indictment alleged that petitioner and his co-defendants conspired to violate 15 U.S.C. 77q(a) (securities fraud), as well as 18 U.S.C. 1014 (fraud in a bank loan application), 18 U.S.C. 1341 (mail fraud), and 18 U.S.C. 1343 (wire fraud). The indictment also contained two substantive counts, charging petitioner with violations of 18 U.S.C. 1014 and 15 U.S.C. 77q(a). The jury acquitted petitioner of the substantive charge under 15 U.S.C. 77q(a), and the government agreed to a dismissal of the charge under 18 U.S.C. 1014 before the jury reached a verdict (Tr. 2761).

[2] Four other defendants, Peter Crosby, Otto Sebold, Leonard James, and C.W. Deaton, were named in the indictment. Upon the government's motion, the proceedings against petitioner were severed before trial. Charges against Deaton were subsequently dropped after he was convicted on six counts of fraud in the United States District Court for the Northern District of Texas and sentenced to 50 years' imprisonment. Sebold and James were convicted of conspiracy, in violation of 18 U.S.C. 371, and securities fraud, in violation of 15 U.S.C. 77q(a). See *United States* v. *James*, 609 F.2d 36 (2d Cir. 1979), cert. denied, No. 79-1115 (Feb. 25, 1980). Co-defendant Crosby was acquitted of all charges.

659, 663-664, 2003). Tri-State, which held itself out as an energy production and exploration company, was in serious financial difficulty at the time. In October 1972, petitioner and two other officers of Tri-State, Leonard James and C.W. Deaton, sought to obtain loans for Tri-State from Bankers Trust Company (Tr. 665, 1368). Initially, the bank rejected the loan request (Tr. 666-667, 1369). Later, however, Tri-State obtained loans totalling $475,000 from the bank, using false documentation, material misrepresentations, and "bogus collateral" (Pet. App. 6a).[3]

2. In obtaining the loans, Tri-State provided the bank with a fraudulent balance sheet that petitioner helped to prepare (Tr. 341, 668-673).[4] The balance sheet listed a $7,500,000 account receivable, based upon a coal sale to a company called Charter Financial, as Tri-State's principal asset (Tr. 344, 349; Gov. Exh. 49, Doc. B-2c). In fact, no such receivable existed; Charter Financial was a shell company without any assets, and the documentation for the account receivable was forged (Pet. App. 6a; Tr. 634-635, 640-647; Gov. Exh. 49, Docs. B-3, B-4, B-5). In addi-

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[3]The original loan of $50,000 was made on October 20, 1972 (J.A. 122a; Gov. Exh. 1). Additional loans were made on November 22, 1972 ($50,000), November 30, 1972 ($100,000), and December 6, 1972 ($275,000) (J.A. 130a, 132a, 134a; Gov. Exhs. 12, 14, 16). These loans were consolidated into a single $475,000 demand note on February 26, 1973 (J.A. 138a; Gov. Exh. 21). See Pet. App. 6a.

Following the initial loan, petitioner gave Raymond Ludwig, the bank branch manager who approved the loan, a $1,500 "gift" (Tr. 676, 1371). Later, he gave Ludwig an additional $2,500 and made two $500 payments to John Keating, another bank officer who also approved the Tri-State loans (Tr. 211, 218, 315-316, 378-379, 1372-1373).

[4]Petitioner, a certified public accountant and law school graduate (Tr. 1774), presented himself to the bank as Tri-State's "financial man" (J.A. 68a; Tr. 598). As the court of appeals observed, petitioner "dress[ed] up Tri-State's financial statement in order to give it the false appearance of a company with a substantial net worth that would generate attractive profits in the future" (Pet. App. 5a).

tion, two uncashed checks totalling $200,000, which were drawn on the personal checking account of a man who previously had been arrested for passing worthless checks, were included in the $264,000 total of "cash on hand" in the balance sheet (Pet. App. 7a; Tr. 668-669, 672, 673). The coal inventories listed in the balance sheet were also overstated (Pet. App. 7a; Tr. 1197).

In addition, the bank received fraudulent projections of future earnings from Tri-State, which petitioner helped to prepare (Tr. 365, 726). Those projections (Gov. Exh. 49, Doc. A-9) were based in substantial part on sham contracts that were supported by forged documents (Pet. App. 8a n.7; Tr. 365-366, 372-373, 667, 722-723, 1109, 1113, 1115, 1174-1175; Gov. Exhs. 49, Doc. B-23; 58) and on an overstatement of coal reserves (Tr. 720).

Further, Tri-State held itself out to the bank as the owner of mineral royalty interests in a producing Kentucky coal mine (Pet. App. 4a-5a, 44a-45a; Tr. 379-381; Gov. Exh. 49, Doc. B-47). In fact, Tri-State leased rather than owned the mine (Tr. 155-167), and while it did briefly conduct a small coal mining operation, it did not follow the usual practice of shipping the mined coal to purchasers (Tr. 156). Instead, Tri-State stockpiled the coal it produced (Tr. 157-158), and then took pictures of the stockpile and freshly painted mining equipment (Tr. 156), presumably for promotional purposes.

3. As the court of appeals stated, "[f]rom the beginning of its relationship with Tri-State, Bankers Trust had made it clear that any loans must be collateralized" (Pet. App. 8a). The bank insisted that Tri-State pledge securities as collateral for its loans (J.A. 14a, 17a, 23a, 31a-34a, 168a-169a; Tr. 246, 254, 305-309; Gov. Exh. 65). The pledged securities were viewed as a source of repayment in the event that Tri-State's projected earnings did not materalize (J.A. 11a; Tr. 239).

In response to the bank's demand, between October 20, 1972 and January 19, 1973, Tri-State pledged stock in six companies.[5] Petitioner, who had substantial business contacts with Bankers Trust prior to his association with Tri-State, served as Tri-State's principal representative with the bank on these and other financial matters (J.A. 14a–15a, 68a–69a; Tr. 247, 540, 598–599).[6]

To effectuate its pledge of securities to the bank, Tri-State executed instruments granting the bank broad powers over the securities. Those instruments gave the bank the right to sell the securities if Tri-State defaulted on its loans (J.A. 124a–127a, 136a, 137a, 140a–143a, 144a–153a, 8a–9a, 21a–23a, 28a–30a, 36a–37a; Gov. Exhs. 7, 8, 19, 20, 28, 29, 37, 38; Tr. 233–234, 281–282, 283–284, 296–299, 313–314). Thus, Tri-State executed in blank "stock powers" that gave the bank the right to "sell, assign, and transfer" the pledged securities and appointed the bank its "attorney to transfer the said stock on the books of [the issuer] with full power of substitution in the premises" (J.A. 124a–127a; Gov. Exhs. 7, 8). Tri-State also executed powers of attorney, applicable to all the stocks pledged, whereby Bankers Trust was "made, constituted and appointed * * * true and lawful attorney [for Tri-State] * * * with power to execute endorsements, assignments or other instruments of conveyance or transfer of certificates

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[5]The stocks were pledged on October 20, 1972 (400,000 shares of American Leisure Corp.); November 10, 1972 (2,000 shares of All States Life Insurance Company); November 22, 1972 (20,000 shares of Marlin Investment Company); December 6, 1972 (100,000 shares of Management Dynamics, Inc.); December 19, 1972 (175,000 shares of General Investment Corporation); and January 19, 1973 (50,000 shares of Satellite Systems Corp.) (J.A. 160a, 168a–169a; Gov. Exhs. 49, Doc. A–7; 65). See Pet. App. 9a n.8. All shares were pledged as collateral for each of the loans. *Ibid.*

[6]Because of the bank's confidence in petitioner, it did less than the customary amount of checking that normally accompanied an extension of credit (J.A. 61a–62a, 71a, 156a; Tr. 430–431, 619–620; Gov. Exh. 48).

of stock or registered securities which it holds or may hold * * *" (J.A. 136a; Gov. Exh. 19). In addition, Tri-State presented corporate resolutions assuring that its agents were empowered to "sell, assign, transfer or dispose of" the stocks that were conveyed to the bank (J.A. 137a, 144a; Gov. Exhs. 20, 30).[7]

From the outset, Bankers Trust insisted that the securities pledged by Tri-State be "good marketable collateral that was not restricted" (J.A. 31a–37a, 13a–14a, 17a, 23a; Tr. 305–315, 245–246, 254, 284). This point was reiterated to petitioner and co-defendant Deaton on a "daily" basis (J.A. 32a; Tr. 307). As described by John Keating (J.A. 33a; Tr. 308):

> The [Tri-State] people were coming into the bank almost on a daily basis, each time they would come in they would be describing various activities of the coal company and the conversations always evolved to the point of the collateral that we were holding and our desires to get New York Stock Exchange collateral.

Keating testified that, when restricted stock is pledged to secure a loan, "it is not marketable in a broad sense" and "the worth of the collateral is substantially reduced, because if you had to sell the stock, you could only do it in dribs and drabs over a long period of time" (J.A. 11a–12a,

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[7]John Keating, the lending officer at Bankers Trust who received the pledged securities in conjunction with these documents, summarized the bank's rights in the collateral as follows (J.A. 22a–23a; Tr. 283): "When you take stock as collateral, there are two ways in which you have the right to sell it; Number 1, you can take stock powers as we did when the American Leisure stock was delivered to the bank. The second way you can do it is to get a blanket form called a power of attorney to endorse securities. This form can be used in lieu of stock powers to cover various amounts of securities * * *." The lending officer added (*ibid.*): "Tri-State Energy * * * is authorizing the bank that they are giving it the right to sell, assign, transfer or dispose of any stocks, bonds, or other securities which the bank may hold as collateral."

94a-95a; Tr. 242-243; see Tr. 1230).[8] Thus, Keating noted (J.A. 13a; Tr. 245):

> obviously the preference of any lending officer was to have unrestricted stock so that if anything went wrong with the loan he would be in a position to sell it right away instead of over an extended period of time.

In response to the bank's continuous requests for high quality marketable securities, Tri-State repeatedly assured the bank that it would supply "good marketable collateral" (J.A. 13a-14a, 17a, 23a, 32a, 33a-34a; Tr. 245-246, 254, 284, 307-309). Contrary to its representations, Tri-State never provided such securities. The securities that it did pledge were "valueless" securities issued by "shell corporations" (Pet. App. 9a; J.A. 85a, 72a-76a, 110a-111a; Tr. 664, 680-687, 820, 892, 1383-1384). Tri-State misled the bank by false representations concerning the value, ownership, and marketability of the securities and took various actions to prevent the bank from determining, through an independent investigation, the true worth of the securities Tri-State had pledged (Pet. App. 4a, 6a, 8a-9a).

4. On October 20, 1972, concurrently with the bank's first ($50,000) loan to Tri-State, Tri-State pledged 400,000 shares of stock issued by American Leisure Corp., a

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[8] Under the Securities Act of 1933, every sale of securities requires registration unless the seller can establish that a statutory exemption is applicable. See Sections 4 and 5 of the Securities Act of 1933, 15 U.S.C. 77d and 77e. One method by which "restricted" securities (securities acquired from the issuer or an affiliate in a non-public transaction) can be sold without registration is by complying with the conditions set forth in Securities and Exchange Commission Rule 144, 17 C.F.R. 230.144, including volume limitations, minimum holding period, manner of sale requirements, and availability of adequate current public information concerning the issuer. Rule 144 also sets forth conditions under which securities held by controlling persons of the issuer can be sold without registration.

"publicly-owned shell" with assets consisting of a pending lawsuit (J.A. 111a, 5a–8a, 110a–112a; Tr. 1384, 222, 228, 233, 1383–1385). This stock had been obtained by Tri-State from Jack Lipsitz, an individual who dealt in what petitioner called "junk stocks" (J.A. 111a; Tr. 1383–1384). Because the restricted nature of the American Leisure stock was apparent on the face of the stock certificate (Gov. Exh. 6),[9] the bank requested that Tri-State replace the stock with marketable collateral (J.A. 14a; Tr. 246). In response, petitioner assured the bank that the restriction was being lifted and that the stock would soon be freely marketable (J.A. 14a, 41a; Tr. 246, 356). In fact, as petitioner well knew (Tr. 1862–1865), that was not the case.[10] Tri-State also agreed to pledge additional marketable securities (J.A. 13a–14a, 31a–33a; Tr. 246, 305–308).

In response to the bank's request for marketable and unrestricted collateral, Tri-State pledged 2,000 shares of stock in All States Life Insurance Company on November 10, 1972 (J.A. 24a–26a, 31a–32a, 65a–66a; Tr. 290–293, 305–306, 580–581; Gov. Exhs. 24–29). This stock, however, was not freely marketable (J.A. 90a–94a, 96a–97a, 110a–111a; Tr. 1212–1216, 1219–1222, 1255–1256, 1383, 1818–1819, 1954). Moreover, contrary to Tri-State's representation that the stock had been acquired for coal rights, it did not own the stock. Instead, the stock had been "rented" for the express purpose of pledging it to the bank as collateral (J.A. 31a–32a, 73a–74a; Tr. 306, 682–683, 1955).

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[9] The certificate stated that the stock was not registered and could not be sold without complying with the registration requirements of the Securities Act of 1933 or obtaining an opinion from American Leisure's counsel that the stock could be sold without registration.

[10] A letter from the president of American Leisure to petitioner (J.A. 166a; Gov. Exh. 49, Doc. B–7), which petitioner used to support his representations to the bank (J.A. 41a; Tr. 355–356), related to the anticipated lifting of restrictions on shares owned only by petitioner personally, not the shares pledged with the bank.

Further, the company had no current assets and the stock was, as petitioner recognized, "without value" (J.A. 72a-74a; Tr. 681-683). To conceal the stock's worthlessness from the bank, petitioner arranged for a broker in the over-the-counter market to place fictitious bid and offer quotations (of $21 and $22 respectively) in the daily "pink sheets" used by the bank to value over-the-counter securities (J.A. 170a-174a, 17a, 76a-77a, 97a-103a, 107a-108a; Gov. Exhs. 146, 147; Tr. 253-254, 687-688, 1269-1278, 1377-1379).[11]

On November 22, 1972, the date on which Tri-State obtained its second loan from the bank, it gave certificates to the bank representing 20,000 shares of Marlin Investment Company (J.A. 28a-29a, 144a-149a; Tr. 296-297, 1095-1096; Gov. Exhs. 36A-D, 37A-C). Although on their face these certificates were registered in the name of Bachelor Investment Company, Tri-State assured the bank that it owned the stock, which it claimed to have received in exchange for coal rights (J.A. 36a; Tr. 313). The stock, however, had been rented by Tri-State from an individual to whom petitioner had stated that the stock was not being

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[11] Petitioner caused the fictitious quotations to appear in the pink sheets for over four months through a friend who operated a stock brokerage firm. The purpose of the sham quotations was to "give a value to" the stock that Tri-State was pledging (J.A. 76a-77a; Tr. 687-688). Petitioner made out a personal check to the brokerage firm so that Tri-State could not be identified with the transaction (*ibid.*). The pink sheet price did not reflect an actual market, as the broker explained, "because this stock was not available, there was no place to buy it" (*ibid.*; see also Tr. 1298). Petitioner admitted full knowledge of the purpose of the fictitious pink sheet quotations. Petitioner's admission was recounted by a federal agent who testified at trial: "Deaton, according to Mr. Rubin, said to him that he wanted the price of All States stock, $21 a share, to appear in the National Quotation Bureau's pink sheets so that the bank or banks could refer to these pink sheets in determining the value or a value for All States stock" (Tr. 1379). Tri-State was attempting at that time to obtain "loans using All States Life Insurance as collateral around the country" (*ibid.*).

used as collateral (J.A. 74a, 112a–115a; Tr. 684, 1394–1399). The bank's subsequent attempts to have the Marlin stock transferred to Tri-State's name were unsuccessful (J.A. 29a, 112a; Tr. 297–298, 1394; Gov. Exhs. 38B, 39).

On December 6, 1972, the date of Tri-State's fourth loan from the bank, Tri-State provided the bank with additional collateral, pledging 100,000 shares of stock in Management Dynamics, Inc., which it represented to be "marketable" (J.A. 26a, 32a–33a; Tr. 293, 307–308).[12] A few days later, however, Management Dynamics discovered it could not account for 900,000 shares, and the Securities and Exchange Commission suspended trading in the stock (J.A. 33a–34a, 82a–83a; Tr. 729–731). Without disclosing this to the bank, petitioner requested that the pledged Management Dynamics shares be released (J.A. 33a–34a, 83a–84a; Tr. 308–309, 730–731). He promised that he would exchange the stock and certain coal rights for New York Stock Exchange collateral by the following Monday (J.A. 33a–34a; Tr. 308–309). Instead, following the bank's release of the stock, petitioner brought the bank 175,000 shares of General Investment Corporation stock (J.A. 27a, 35a, 66a; Tr. 294–295, 310, 581; Gov. Exhs. 32, 33A–Y), which he represented to be "marketable" and unrestricted (Tr. 310), but which in fact was restricted stock (J.A. 168a; Tr. 1480, 1498; Gov. Exh. 57).

By this time Keating had become "quite disturbed" because Tri-State had failed to furnish New York Stock Ex-

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[12] In contrast to the other stocks pledged by Tri-State, there was a market for Management Dynamics stock (Tr. 1401). However, the shares that Tri-State pledged were restricted (Gov. Exh. 196; Tr. 2073). The same day that Tri-State pledged this restricted stock, John Keating prepared a memorandum stating that the bank had advanced $475,000 secured by "marketable securities as lien collateral" (J.A. 50a, 154a; Tr. 396; Gov. Exh. 47).

change collateral, and he conveyed his concern to petitioner (J.A. 35a; Tr. 311). To calm the bank's growing concerns about the adequacy of the collateral, Tri-State pledged 50,000 shares of Satellite Systems, Corp. on January 19, 1973 (J.A. 27a–28a, 35a, 66a; Tr. 295, 311–312, 581; Gov. Exhs. 34, 35). According to Keating, either petitioner or C.W. Deaton, the Secretary-Treasurer of Tri-State, brought the stock into the bank and stated (J.A. 36a; Tr. 312–313):

> Here is a stock, now you don't have to be asking all the time for New York Stock Exchange collateral, because while this isn't New York Stock Exchange collateral, here is collateral for you that is worth $1 million because we are at 50,000 shares, $20 a share.
>
> * * * This stuff is readily marketable, it is not restricted, all the requests that you have should be more than satisfied by this particular piece of stock.

To support this claim, Tri-State gave Keating a clipping from the International Herald Tribune purporting to show that Satellite Systems stock was trading at $20 to $20.50 per share (J.A. 35a–36a, 51a–52a, 78a–80a, 166a–167a; Tr. 311–312, 410–411, 723–724; Gov. Exh. 49, Doc. B–58). As petitioner knew, the clipping was not a report of genuine stock exchange transactions, but was an advertisement that had been placed in the financial section of the paper by one of Tri-State's cohorts to give the false appearance of a market (J.A. 78a–80a; Tr. 723–725, 893).[13] Moreover, contrary to representations made to the bank (Tr. 313), the stock was restricted and was not even owned by Tri-State, but had been "rented" (J.A. 55a–56a, 74a, 80a–81a,

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[13] The advertisement appeared on the same page of the newspaper that reported stock market quotations, and purported to show current bid and offer prices. The bank was completely deceived by this document, believing that it had received one million dollars worth of marketable securities—50,000 shares of stock "traded on a London OTC exchange for approximately $20" (J.A. 165a; Gov. Exh. 49, Doc. A–8).

112a-115a, 117a-118a; Tr. 421-423, 684, 725-726, 1394-1399, 1403-1404), and was conveyed to Tri-State by Peter Crosby, a man who petitioner then knew was a fugitive (J.A. 75a-76a; Tr. 684-686).

At the same time that Tri-State was pledging worthless securities to Bankers Trust to obtain $475,000 in loans, Owen J. Oons, purportedly acting as Tri-State's attorney, was pledging stock in the same companies as collateral to secure bank loans in several other states. Through Oons' efforts, Tri-State obtained an additional $350,000 to $500,000 in loans (J.A. 81a, 107a-108a; Tr. 727, 1379, 1980-1984).

5. By January 1973, although the bank was confident that the collateral was sufficient to cover the loans (J.A. 165a; Gov. Exh. 49, Doc. A-8), it was concerned about Tri-State's deteriorating financial condition and its failure to live up to its projected performance. Keating learned that, despite the $475,000 in loans Tri-State had obtained from Bankers Trust and the company's purported net worth and projected income, the company's checks frequently were being returned for insufficient funds (Gov. Exhs. 41, 43, 49, Docs. B-10a, B-10b; Tr. 358). He also discovered that Tri-State had an unpaid $12,000 overdraft outstanding at Chemical Bank that had been forwarded to that bank's legal department for collection (Tr. 401-402).[14] When Keating confronted petitioner about the overdraft, petitioner denied knowing that a lawsuit was contemplated and stated that he thought that the Chemical Bank matter had been cleared up (Tr. 402).

In January and February 1973, Keating requested the bank's credit department to check with Dun and

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[14] At the time Tri-State opened its account at Bankers Trust, the bank was unaware that Tri-State had an account at Chemical Bank (J.A. 159a; Tr. 401-403; Gov. Exh. 48).

Bradstreet and the International Stock Exchange in London on the various companies whose stocks had been pledged as collateral by Tri-State (J.A. 52a–54a; Tr. 412–414; Gov. Exh. 49, Docs. A–34a, A–38, B–39, B–51, B–35b, A–44, A–25, A–37). At the same time, Keating attempted to insure that the bank had sufficient documentation on the collateral so that it could sell the collateral if necessary (J.A. 52a; Tr. 412).[15]

On February 26, 1973, Bankers Trust consolidated the loans into a single demand note (J.A. 138a–139a; Gov. Exh. 21). On the same day that the demand note was executed, Leonard James, Tri-State's president, advised Keating that Tri-State had coal ready to be shipped but that deliveries had been temporarily halted by a strike (Tr. 426). In fact there was no strike (Tr. 173), and Tri-State could not realistically have hoped to repay the loans because its mine had been shut down.[16] Two days after the demand note was executed, the bank received an inquiry from the Department of Justice asking for information about Tri-State (Tr. 247; Gov. Exh. 49, Doc. B–16) and a subpoena to produce all records relating to the loans (Tr. 434; Gov. Exh. 49, Doc. A–3).

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[15] Despite its growing concerns about Tri-State's financial condition, the bank believed that the collateral it received, particularly the Satellite Systems stock claimed to be worth $1,000,000, would provide complete protection in the case of a default. See J.A. 158a–159a; Gov. Exh. 48: "Additional information has recently caused us to re-evaluate our thinking on this credit. We were recently informed by William Powderly that an unresolved overdraft was outstanding at the Chemical Bank. We had no knowledge that an account at Chemical existed when the account opened. * * * In addition to this unpleasantness, the firm despite our $475M advance is still in a very tight cash position, and we have had occasion to return a number of checks over the past two weeks. * * * As additional support for our loan, we have received an additional $1MM in marketable securities thus bringing our collateral picture to $1.7MM and giving us, what we feel, is adequate protection."

[16] Deaton's brothers, who managed the mine, had left town, and the mine's equipment had been repossessed (Tr. 163–164, 173, 206, 209).

On March 5, 1973, the bank sent a letter to Tri-State demanding repayment in full and explaining that unless payment was tendered in three days the bank would "commence selling the collateral we hold without any further separate notice" (J.A. 60a; Tr. 428; Gov. Exh. 49, Doc. A-1). Tri-State failed to make repayment (J.A. 60a; Tr. 428). Because the collateral pledged by Tri-State was virtually worthless, the bank was able to recover only $2,500 of the $475,000 loan (plus interest and expenses) that it believed had been secured by $1,700,000 of marketable securities (Pet. App. 9a, 11a; J.A. 88a, 165a; Tr. 1129-1130; Gov. Exh. 49, Doc. A-8).[17]

6. Following petitioner's conviction on the conspiracy count of the indictment, the court of appeals affirmed (Pet. App. 34a). In rendering its judgment, the court did not discuss petitioner's contention that Section 17(a) of the Securities Act of 1933 does not extend to fraudulent pledges (Pet. App. 34a). The court apparently relied on its prior decision in *United States* v. *Gentile*, 530 F.2d 461 (2d Cir.), cert. denied, 426 U.S. 936 (1976), which had held that fraudulent pledges are prohibited by Section 17(a).

SUMMARY OF ARGUMENT

A. Petitioner does not deny that he conspired to commit fraud through false representations concerning stock that he and his co-conspirators pledged with Bankers Trust Company. Nor does he deny that the stock certificates were "securities." Rather, he contends that the fraud he conspired to commit is beyond the reach of Section 17(a) of

[17] After signing a confession of judgment against himself for the amount of the unpaid loans, petitioner filed a petition in bankruptcy (Pet. App. 11a; Tr. 1924). Reviewing its collateral situation, the bank restated its understanding that "[a]ll stock except American Leisure Corp. was not supposed to be restricted" (J.A. 168a-169a; Gov. Exh. 65).

the Securities Act of 1933, 15 U.S.C. 77q(a), because his pledge transactions did not satisfy the statutory definition of an "offer" or "sale" of securities. 15 U.S.C. 77b(3). Petitioner argues that he merely conveyed a "security interest that entitle[d] the pledgee to sell the stock on default," and not "ownership" or "title" (Br. 10, 17). In response, we submit that "this is a case in which the meaning of [the] statute may be determined by the admittedly old-fashioned but nonetheless still entirely appropriate 'plain meaning' canon of statutory construction." *United States* v. *Clarke*, No. 78-1693 (Mar. 18, 1980), slip op. 1.

Section 17(a) forbids all fraudulent practices in an "offer" or "sale" of securities. The term "sale" is broadly defined to "include every * * * disposition of * * * [an] interest in a security, for value." The term "offer" is defined in equally broad terms, including "every attempt * * * to dispose of * * * [an] interest in a security, for value." 15 U.S.C. 77b(3). By transferring securities to the bank with stock powers and powers of attorney entitling it to sell those securities for its own benefit upon default, petitioner clearly conveyed an "interest" in the securities. "At the very least," he "attempt[ed] to dispose" of an interest in securities. *United States* v. *Naftalin*, 441 U.S. 768, 773 (1979). And since the bank would not part with its money without a pledge of securities, it is plain that the "value" that the bank gave depended on obtaining an interest in the securities.

In short, considering the plain meaning of the words used by Congress, there is no room to doubt that petitioner's fraud occurred in an "offer" and "sale" of securities. "There is no requirement that title pass" to constitute an offer or sale. *United States* v. *Gentile*, 530 F.2d 461, 466 (2d Cir.), cert. denied, 426 U.S. 936 (1976).

B. When Congress enacted the Securities Act in 1933, it was well established that a pledgee receiving stock as col-

lateral obtained a substantial legal "interest" in the stock for "value." Congress could not have been unaware of this settled doctrine. Under legal principles generally recognized in 1933, a pledgee obtained a "special property" interest in pledged securities, entitling him to possession of the securities and empowering him to sell them without judicial process in the event of a default. The pledgee's legal interest in the collateral was unaffected by the running of the statute of limitations on the underlying debt or by the pledgor's discharge in bankruptcy. The pledgee's legal interest also prevailed over that of third parties claiming prior ownership rights in the securities. It was well established when Congress passed the Securities Act that a pledgee of negotiable securities ordinarily obtained the legal status of a bona fide "holder" or "purchaser" for value. If Congress had intended to exclude the substantial legal interests of a pledgee, it surely would not have written the statutory sale definition to apply to "every" disposition of an "interest" in a security for value.

C. The legislative history of the Securities Act of 1933 also supports the statute's plain meaning. Congress intended the definitions of "sale" and "offer" to be "expansive" ones. *United States* v. *Naftalin*, *supra*, 441 U.S. at 773. In addition, Congress adopted as its model the definition of "sale" prescribed in the Uniform Sale of Securities Act of 1929. The sponsors of the Uniform Act drafted that definition to reach pledge transactions, and the judicial interpretation was in accord. *Cecil B. De Mille Productions, Inc.* v. *Woolery*, 61 F.2d 45 (9th Cir. 1932). Because Congress incorporated this definitional language from the Uniform Sale of Securities Act of 1929, the Court's observation in *Lorillard* v. *Pons*, 434 U.S. 575, 581 (1978), is fully applicable here: "where, as here, Congress adopts a new law incorporating sections of a prior law, Congress

normally can be presumed to have had knowledge of the interpretation given to the incorporated law * * *."

D. The "policy" arguments advanced by petitioner (Br. 20–26) to curtail the express terms of the statute are insubstantial. The federal securities laws were intended to protect "honest business" as well as "investors" and to "help set the economy on the road to recovery" during the depression. *United States* v. *Naftalin*, *supra*, 441 U.S. at 775–776. In furtherance of this purpose, these statutes were designed to "protect * * * the national banking system," and to eliminate securities practices that could "prevent the fair valuation of collateral for bank loans and/or obstruct the effective operation of the national banking system * * *" (15 U.S.C. 78b).

It is irrelevant that petitioner's scheme injured a bank rather than an individual investor. As this Court held in *United States* v. *Naftalin*, *supra*, 441 U.S. at 776, the Securities Act of 1933 was designed to protect "financial intermediaries" as well as investors. It would also be irrelevant if the victim of petitioner's fraud had assumed only a "commercial risk" and not an "investment risk." Nothing on the face of the statute suggests that its coverage should be narrowed by reference to "undefined categor[ies]" such as investment risk and commercial risk. See *United States* v. *Culbert*, 435 U.S. 371, 380 (1978). Congress has specified the context in which Section 17(a) applies—"every" transaction in which an "interest" in a security is conveyed for "value." The "investment risk"/"commercial risk" dichotomy that petitioner suggests offers no assistance in applying that statutory standard. In any event, the dichotomy that petitioner relies on is an artificial one. Banks parting with their money on the express understanding that marketable securities will be pledged to collateralize a loan assume risks that are comparable to those of investors.

Petitioner's contention that fraudulent pledges are of primary concern to the states, and not the federal government (Br. 25–26), is refuted by the legislative history of the Securities Acts Amendments of 1975, Pub. L. No. 94–29, 89 Stat. 97. The legislative history of those amendments shows that fraudulent pledges are a primary means by which participants in organized crime convert otherwise unmarketable securities into cash, often for reinvestment into other organized criminal activities. These transactions, involving worthless, counterfeit and stolen securities, have caused serious financial injury to many federally insured banking institutions. Fraudulent pledges are carried on by organized crime on a nationwide and often on an international basis. Local authorities are powerless to prevent fraudulent practices occurring on such a scale.

ARGUMENT

SECTION 17(a) OF THE SECURITIES ACT OF 1933 PROHIBITS FRAUD IN THE PLEDGE OF SECURITIES

The jury found petitioner guilty of conspiracy to violate various federal antifraud statutes, including Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), a provision "'designed to protect not only the investing public but at the same time to protect honest corporate business.'" *United States* v. *Naftalin*, 441 U.S. 768, 776 (1979). In this Court, petitioner does not dispute that he conspired to defraud Bankers Trust Company through false representations concerning the value, marketability and ownership of the collateral that was pledged with the bank. Nor does he deny that the stocks that he pledged were "securities" within the meaning of Section 2(1) of the Securities Act of 1933, 15 U.S.C. 77b(1), or that the stocks were required

by the bank as a prerequisite for extending almost one-half million dollars in loans. Rather, he contends (Br. 12–20) that Section 17(a) does not prohibit fraud in the pledge of securities, and, therefore, his conduct could not have violated the statute. The limiting construction that petitioner suggests, however, is plainly inconsistent with the literal terms of the statute and "would create a loophole in the statute that Congress simply did not intend to create." *United States* v. *Naftalin*, *supra*, 441 U.S. at 777.

A. Fraud in the Pledge of Securities as Collateral for a Loan Is Forbidden by the Plain Language Used by Congress in the Securities Act of 1933

1. As this Court repeatedly has emphasized in construing the federal securities laws, "'[t]he starting point in every case involving construction of a statute is the language itself.'" *International Brotherhood of Teamsters* v. *Daniel*, 439 U.S. 551, 558 (1979), quoting *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975) (Powell, J., concurring). See also *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, No. 77–1645 (Nov. 13, 1979), slip op. 4; *Aaron* v. *SEC*, No. 79–66 (June 2, 1980), slip op. 9; *United States* v. *Clarke*, No. 78–1693 (Mar. 18, 1980), slip op. 1. Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), broadly forbids any person, "in the offer or sale of any securities," to engage in any fraudulent practice.[18] Section 17(a)(1) forbids any person to employ any device, scheme or artifice to defraud in an offer or sale of securities. Section 17(a)(2) forbids any person to obtain money or property by means of any untrue statement or

[18]The indictment in this case charged that petitioner conspired to commit fraudulent practices "in the offer and sale" of securities, and that the conspiracy was carried out through the pledges made with Bankers Trust Company. Indictment, Count 1, ¶ 18.

omission to state a material fact needed to avoid deception in an offer or sale of securities. And Section 17(a)(3) forbids any person to engage in any practice in an offer or sale of securities that operates or would operate as a fraud or deceit on the purchaser.[19]

The statutory terms "offer" and "sale" are, in turn, defined in comprehensive terms. Under Section 2(3) of the Act, 15 U.S.C. 77b(3), the term "sale" is expressly defined to "include every contract of sale or disposition of a security *or interest in a security*, for value" (emphasis supplied). The term "offer" is defined in equally broad terms. Under Section 2(3), an "offer" is defined to include "every attempt * * * to dispose of * * * a security *or interest in a security*, for value" (emphasis supplied).[20] Thus, according to the plain meaning of the terms used by Congress, the statute extends to every disposition of an "interest" in a security for value and every "attempt" to dispose of an "interest" in a security for value. As this Court noted in *United States* v. *Naftalin*, *supra*, 441 U.S. at 773, these are "expansive" terms, which Congress "expressly intended to define broadly * * *." See also *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 467 n.8 (1969); I L. Loss, *Securities Regulation* 512 & nn.162–163 (2d ed. 1961).

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[19] As this Court noted in *United States* v. *Naftalin*, *supra*, 441 U.S. at 773–774, "while impact upon a purchaser may be relevant to prosecutions brought under § 17(a)(3), it is not required for those brought under § 17(a)(1). * * * Each * * * prohibition is meant to cover additional kinds of illegalities * * *."

[20] As originally enacted, the terms "sale" and "offer to sell" were included in a single definitional sentence. See 48 Stat. 74. In 1954, Congress amended the Act to provide separate definitions of "offer" and "sale." To preserve existing law, Section 17(a) was amended to include the term "offer." See 68 Stat. 683, 686; S. Rep. No. 1036, 83d Cong., 2d Sess. 4 (1954).

Giving the words used by Congress "their ordinary, contemporary, common meaning" (*Perrin* v. *United States*, No. 78–959 (Nov. 27, 1979), slip op. 5), it is clear that petitioner and his co-conspirators offered and sold securities. Petitioner concedes (Br. 17) that he conveyed to the bank a "security interest that entitle[d] the pledgee to sell the stock on default." That "interest" was formalized by the stock powers and powers of attorney that petitioner and his co-conspirators delivered to the bank in conjunction with the securities, which gave the bank the legal right to sell or assign the securities. The bank also obtained sole possession of the securities so that it could enforce its interest through prompt liquidation. Of course, the bank gave value for its interest in the securities when it extended $475,000 in loans. That money was furnished to petitioner and his co-conspirators on the express condition that they provide the bank with "good marketable securities."[21] In sum, petitioner and his co-conspirators "sold" securities because they disposed of an "interest" in the securities for value.[22] "At the very least," they offered securities because they "attempt[ed] to dispose" of an interest in the securities for value. *United States* v. *Naftalin*, *supra*, 441 U.S. at 773. Thus, although petitioner argues that the statute should be narrowed to exclude

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[21] As the court of appeals emphasized: "From the beginning of its relationship with Tri-State, Bankers Trust had made it clear that any loans must be collateralized" (Pet. App. 8a).

[22] Indeed, the pledges, coupled with stock powers and powers of attorney authorizing the bank to sell the securities, constituted a "contract" to sell under specified circumstances (default), and thus fell within the statutory definition of "sale" for an independent reason. The fact that the sale depended on the occurrence of a future contingency is irrelevant, since many conventional securities contracts (including stop loss orders, limit orders, and options) are contingent in nature. See *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 750–751 (1975) (options); see also *Kerbs* v. *Fall River Industries, Inc.*, 502 F.2d 731, 738–739 (10th Cir. 1974).

fraudulent pledges, "[n]othing on the face of the statute supports this reading of it." *Id.* at 772.

2. Petitioner argues that the word "sale" cannot apply to the transfer of a "security interest" for value because the word "sale" implies "transfer of title or ownership* * *" (Br. 10). In making this argument, petitioner relies on dictionary definitions of the term "sale" (*id.* at 16). However, "[t]he short answer is that Congress did not write the statute that way." *United States* v. *Naftalin*, *supra*, 441 U.S. at 773. Congress prescribed its own definition of the word "sale," which expressly includes "every" transfer of an "interest" in a security for value, as well as transfers of title. See *United States* v. *Gentile*, 530 F.2d 461, 466 (2d Cir.), cert. denied, 426 U.S. 936 (1976):

> The term "sale" is defined in the Securities Act of 1933, § 2(3), 15 U.S.C. § 77b(3) to include "every contract of sale or disposition of a security or interest in a security, for value." There is no requirement that title pass to constitute a "sale" within the meaning of the statute. Indeed, to read "sale" so restrictively would render superfluous the latter two disjunctive phrases in the statutory definition. Since Gentile obviously obtained value in the form of bank loans for his pledge of stock, his actions fall within the strict construction that we apply to criminal statutes.

See also *Blue Chip Stamps* v. *Manor Drug Stores*, *supra*, 421 U.S. at 733 n.5; *Kerbs* v. *Fall River Industries, Inc.*, *supra*, 502 F.2d at 739; *Mansbach* v. *Prescott, Ball & Turben*, 598 F.2d 1017, 1028–1029 (6th Cir. 1979). As the Seventh Circuit correctly observed in *Dasho* v. *Susquehanna Corp.*, 380 F.2d 262, 266 (7th Cir.), cert. denied, 389 U.S. 977 (1967) (discussing the definition of "sale" in the Securities Exchange Act of 1934), "[t]his broad language indicates an intention by Congress that the words 'purchase' and 'sale' are not limited to transactions ordinarily governed by the commercial law of sales. The

purpose is evidently to make control of securities transactions reasonably complete and effective to accomplish the purposes of the legislation."

By ignoring the fact that Congress has prohibited fraud in the process of disposing of an "interest" in securities, as well as fraud in the process of transferring ownership, petitioner's argument clashes with the basic rule that "[i]n construing a statute we are obliged to give effect, if possible, to every word Congress used." *Reiter* v. *Sonotone Corp.*, 442 U.S. 330, 339 (1979). Petitioner's interpretation violates "the elementary canon of construction that a statute should be interpreted so as not to render one part inoperative." *Colautti* v. *Franklin*, 439 U.S. 379, 392 (1979). Such an interpretation is particularly inappropriate under an antifraud statute that was intentionally drafted in comprehensive terms to eliminate fraud in all aspects of securities transactions.[23] See *United States* v. *Naftalin*, *supra*, 441 U.S. at 774: "There is * * * 'no warrant for narrowing alternative provisions which the legislature has adopted with the purpose of affording added safeguards.'"[24]

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[23] The statutory definition embraces three categories of "sale" transactions—contracts of sale, dispositions of securities for value, and dispositions of interests in securities for value. The broad nature of the definition is shown by Congress' use of the word "include," which demonstrates that the transactions specifically enumerated are not exclusive. See generally *SEC* v. *National Securities, Inc.*, *supra*, 393 U.S. at 467 n.8. See also I L. Loss, *Securities Regulation*, *supra*, at 512–513 & n.162.

[24] Petitioner's suggestion (Br. 17) that a "security interest" is of lesser economic significance than other interests is also refuted by the plain meaning of the statute. The statute is not limited to particular economic interests. It extends to "every" interest, and there is nothing unreasonable about applying the statute at face value. See *United States* v. *Rutherford*, 442 U.S. 544, 555 (1979): "Only when a literal construction of a statute yields results so manifestly unreasonable that they could not fairly be attributed to congressional design will an exception to statutory language be judicially implied." See also *TVA* v. *Hill*, 437 U.S. 153, 187–188 & n.33, 194–195 (1978).

Nor can petitioner find support for his restrictive reading of the Act in the absence of the word "pledge" in the definition. The statute employs generic language—embracing "every" interest in a security—which covers a pledgee's legal interest and other interests as well. Congress did not define the term "sale" by attempting to prescribe an exhaustive list of transactions intended to be covered. Thus, the absence of the word pledge "provides no basis for concluding that Congress intended to exclude [that type of transaction] from the Act's coverage." *Tcherepnin* v. *Knight*, 389 U.S. 332, 344 (1967). This Court and the lower federal courts repeatedly have recognized that a wide variety of transactions not mentioned by name—including mergers,[25] issuance of stock,[26] short sales,[27] puts, calls and options,[28] and exchanges of shares[29]—are encompassed by the generic "sale" definitions used in the federal securities laws.

In sum, the statutory definitions of "sale" and "offer," broadly embracing every disposition of an interest in a security for value and every attempt to dispose of an inter-

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[25]*SEC* v. *National Securities, Inc.*, *supra*, 393 U.S. at 465–468; *Smallwood* v. *Pearl Brewing Co.*, 489 F.2d 579, 591 (5th Cir.), cert. denied, 419 U.S. 873 (1974); *Vine* v. *Beneficial Finance Co.*, 374 F.2d 627, 634 (2d Cir.), cert. denied, 389 U.S. 970 (1967); *Dasho* v. *Susquehanna Corp.*, *supra*, 380 F.2d at 266–267.

[26]*Schoenbaum* v. *Firstbrook*, 405 F.2d 215, 219–220 (2d Cir. 1968), cert. denied, 395 U.S. 906 (1969); *Hooper* v. *Mountain States Securities Corp.*, 282 F.2d 195, 202–203 (5th Cir. 1960), cert. denied, 365 U.S. 814 (1961).

[27]*United States* v. *Naftalin*, *supra*, 441 U.S. at 776.

[28]*Blue Chip Stamps* v. *Manor Drug Stores*, *supra*, 421 U.S. at 750–751.

[29]*Bryan* v. *Brock & Blevins Co.*, 490 F.2d 563, 568 (5th Cir.), cert. denied, 419 U.S. 844 (1974); *Swanson* v. *American Consumer Industries, Inc.*, 415 F.2d 1326, 1330 (7th Cir. 1969); *Knauff* v. *Utah Construction & Mining Co.*, 408 F.2d 958, 961 (10th Cir.), cert. denied, 396 U.S. 831 (1969).

est for value, include the security interest conveyed to the bank by petitioner. There is no warrant for implying exceptions to the broad language prescribed by Congress to eliminate fraud in all phases of securities transactions. See *United States* v. *Naftalin*, *supra*, 441 U.S. at 772, 774; *United States* v. *Culbert*, 435 U.S. 371, 373–374, 380 (1978).[30]

B. It Was Well Established in 1933 That a Pledgee Receiving Securities as Collateral for a Loan Obtained an "Interest" in the Securities for "Value"

While the "plain meaning" of the definition of the term sale in the Securities Act is "so unambiguous as to suggest that 'further inquiry may be unnecessary'" (*Aaron* v. *SEC*, *supra*, slip op. 9, quoting *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 201 (1976)), an examination of legal principles established in 1933 fortifies the conclusion that petitioner's securities transactions fall within the statutory definition. That examination shows general rec-

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[30] While petitioner relies on the sale definition in the Securities Exchange Act of 1934 (Br. 14), the language used in that definition is not the same as that used to define the words "offer" and "sale" in the Securities Act of 1933. See, *e.g.*, *Blue Chip Stamps* v. *Manor Drug Stores*, *supra*, 421 U.S. at 733 n.5; see also *id.* at 750–751 n.13; note 36, *infra*. In particular, the sale definition in the Securities Act of 1933 extends to every disposition of an "interest" in a security for value. In contrast, the definition of sale in the Securities Exchange Act of 1934 includes "any contract to sell or otherwise dispose of" a security. 15 U.S.C. 78c(a)(14). The Securities Exchange Act definition does not expressly refer to the transfer of an "interest" in securities. For that reason, even if pledges were not viewed as sales under the Securities Exchange Act, that would not be dispositive of the question presented in this case—whether pledges are offers or sales under the Securities Act. Nonetheless, those lower court decisions holding that a pledge of securities is a sale under the Securities Exchange Act provide *a fortiori* support for application of the Securities Act to such transactions, in view of the more expansive language in the Securities Act definition. See note 45, *infra*.

ognition at the time when the Securities Act was enacted that a pledgee receiving securities as collateral for a loan obtained a substantial "interest" in the securities for "value."

1. By 1933, it was generally recognized that a pledgee receiving securities as collateral for a loan obtained a substantial legal "interest" in the securities.[31] That interest was described as a "special property" in the securities. See *Jones on Collateral Securities* 4–6, 12, 190–191 (1912); J. Story, *Commentaries on the Law of Bailments* 241 (1863); *Yeatman* v. *Savings Institution*, 95 U.S. 764, 766 (1877).

The "special property" of the pledgee entailed a bundle of specific legal rights and interests. In the case of collateral securities, the pledgee obtained "the interest of the pledgor, subject to the latter's power to redeem" if the loan was repaid. *Restatement of the Law of Security* § 2, comment at 14 (1941). The pledgee could compel endorsement of collateral securities *(ibid.)*; retain any dividends or profits stemming from the pledged securities as additional collateral (*id.* at § 3); assign the pledged securities and secured debt (*id.* at § 29); and (unlike a lien holder) sell the collateral following default without judicial foreclosure (*id.* at § 48). The pledgee's legal rights in collateral securities were unaffected by either the running of the

[31] In 1933, the word "interest" was recognized as being "[t]he most general term that can be employed to denote a property in lands or chattels. * * * More particularly it means a right to have the advantage accruing from anything; any right in the nature of property, but less than title * * *." *Black's Law Dictionary* 646 (2d ed. 1910). See also *The Oxford English Dictionary* 393 (1933), defining the word "interest" as a "legal concern in a thing; esp. right or title to property, or to some of the uses or benefits pertaining to property." Accord, *Webster's New International Dictionary of the English Language* 1125 (1930), defining "interest" as a "right, title, share, or participation in a thing * * * specif., participation in advantage, profit, and responsibility * * *." Thus, "interest" includes ownership or title, but is not so limited.

statute of limitations on the claim underlying the pledge or a discharge of the claim in bankruptcy (*id.* at § 47).

2. It was also well established prior to 1933 that the pledgee's "special property" interest in negotiable securities obtained as collateral without notice of adverse claims was superior to the interest of third parties asserting ownership of the securities—*i.e.*, the pledgee received "a legal interest sufficient to invoke the rule protecting bona fide purchasers." 49 C.J. *Pledges* § 64 (1930). The decisions of this Court acknowledged that rule. See, *e.g.*, *Railroad Co.* v. *National Bank*, 102 U.S. 14, 25–26 (1880):

> [I]t may be regarded as settled in commercial jurisprudence * * * that where negotiable paper * * * is transferred, by indorsement, as collateral security for a debt created * * * at the time of transfer * * * the holder who takes the transferred paper * * * without notice * * * of any defence thereto, is held to have received it in due course of business, and * * * becomes a holder for value * * *.

Accord, *Restatement of the Law of Security*, *supra*, at § 35(b); see also *id.* at 109 (illustration). This concept was adopted in the earliest commercial law codifications in this country. For example, under the Uniform Negotiable Instruments Law, approved by the National Conference of Commissioners on Uniform State Laws in 1896 and subsequently adopted in every state in the Union prior to 1933 (see National Conference of Commissioners on Uniform State Laws, *Handbook and Proceedings* 504, 517 (1933) (hereinafter *Handbook and Proceedings*)), a pledgee receiving negotiable instruments was deemed a holder for value. See Uniform Negotiable Instruments Act §§ 25, 27, 52, 57 (reproduced in 5 Uniform Laws Annotated (1943)). Similarly, under the Uniform Stock Transfer Act, which was approved in 1907 and adopted in 23 states prior to 1933 (see *Handbook and Proceedings*,

supra, at 503, 517), a "pledgee" was deemed a "purchaser" for "value" if he received stock collateral for a contemporaneous or antecedent debt. See Uniform Stock Transfer Act § 22 (reproduced in 6 Uniform Laws Annotated (1922)).[32] Summarizing this body of law in 1914, the Seventh Circuit observed in *National City Bank of Chicago* v. *Wagner*, 216 F. 473, 481–482 (7th Cir. 1914):

> By the great weight of authority at common law, both in England and the United States, and now by the Uniform Negotiable Instruments Act, in force in 46 jurisdictions, one who takes commercial paper as collateral security for a preexisting debt is deemed to have given value. * * * As further evidencing the mercantile view of the character of documents such as stock certificates, bills of lading, and warehouse receipts, it may be noted that under the provisions of the Uniform Warehouse Receipts Act, in force in 30 jurisdictions, * * * and the [Uniform] Stock [Transfer] Act, in force in 9 jurisdictions, purchaser for value is defined as including one taking such documents as collateral for a pre-existing debt.

Not only were the foregoing principles of commercial law well established in 1933, when the Securities Act was passed by Congress, but they continue to be recognized

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[32] Likewise, under the Uniform Warehouse Receipts Act, which was approved in 1906 and adopted in 44 states by 1933 (*Handbook and Proceedings*, *supra*, at 504, 518), a "pledgee" who extended credit secured by warehouse receipts was deemed a "purchaser" for value. See Uniform Warehouse Receipts Act §§ 37–41, 58 (reproduced in 3 Uniform Laws Annotated (1959)). The same rule was expressed in § 1 of the Uniform Conditional Sales Act, approved in 1918 and adopted in 9 states by 1933 (*Handbook and Proceedings*, *supra*, at 503, 515); in § 53 of the Uniform Bills of Lading Act, approved in 1909 and adopted in 29 states by 1933 (*Handbook and Proceedings*, *supra*, at 503, 515); and in § 76 of the Uniform Sales Act, approved in 1906 and adopted in 32 states by 1933 (*Handbook and Proceedings*, *supra*, at 504, 517) (reproduced in 2 Uniform Laws Annotated (1922), 4 Uniform Laws Annotated (1922), and 1A Uniform Laws Annotated (1950), respectively).

today in every state (except Louisiana) under the provisions of the Uniform Commercial Code. The Code, which was in effect in New York at the time of petitioner's pledges, provides expressly that a "pledgee" is a "purchaser" and that a pledgee gives "value" when he extends credit or receives collateral for a pre-existing debt. See N.Y. U.C.C. (62½–Pt. 1) § 1–201(32), (33), (44) (McKinney 1964). See also *id.* at §§ 8–301, 8–302, 8–308 (Pt. 3) (bona fide purchaser rule protects securities purchasers who obtain securities for value without notice of adverse claims).[33] A bank pledgee may resell the collateral in any commercially reasonable manner. See *id.* at § 9–504 (Pt. 3).

In sum, looking at the "ordinary meaning" of the terms used by Congress "at the time Congress enacted the statute" (*Perrin* v. *United States*, *supra*, slip op. 5), it is clear that petitioner's pledge of securities was a disposition of an "interest" in those securities for "value." In other words, at the time when Congress drafted the definition of "sale" in the Securities Act of 1933, which expressly includes "every" disposition of an interest in a security for value, it was well established that a pledge was precisely such a disposition.[34]

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[33] See E. Peters, *A Negotiable Instruments Primer* 35 (2d ed. 1974): "A bank which has taken a pledge interest in deposited instruments as security for a loan is a purchaser for value to the extent of the pledgor's outstanding indebtedness * * *." For a recent application of New York's "bona fide purchaser" rule to a bank pledgee obtaining collateral securities, see *Gutekunst* v. *Continental Ins. Co.*, 486 F.2d 194 (2d Cir. 1973).

[34] See *Lorillard* v. *Pons*, 434 U.S. 575, 583 (1978), quoting *Standard Oil Co.* v. *United States*, 221 U.S. 1, 59 (1911): "'where words are employed in a statute which had at the time a well-known meaning at common law or in the law of this country they are presumed to have been used in that sense unless the context compels to the contrary.'" See also *Cannon* v. *University of Chicago*, 441 U.S. 677, 696–697 (1979).

C. The Legislative History of the Securities Act of 1933 Supports the View That a Pledge of Securities is a Disposition of an Interest in Securities for Value and Thus Falls Within the Statutory Definition of "Sale"

Petitioner contends (Br. 15) that the legislative history of the Securities Act of 1933 does not address the question whether a pledge of securities falls within the Act's generic definition of sale. Even if that were the case, the silence of the legislative history would not alter the plain meaning of the terms used by Congress. As this Court recently noted in *Harrison* v. *PPG Industries, Inc.*, No. 78–1918 (May 27, 1980), slip op. 13:

> [I]t would be a strange canon of statutory construction that would require Congress to state in committee reports or elsewhere in its deliberations that which is obvious on the face of a statute. In ascertaining the meaning of a statute, a court cannot, in the manner of Sherlock Holmes, pursue the theory of the dog that did not bark.

In short, "[p]etitioner's argument would permit an omission in the legislative history to nullify the plain meaning of a statute." *Standefer* v. *United States*, No. 79–383 (June 9, 1980), slip op. 9–10 n.12.[35]

In fact, however, the legislative history is not silent. It provides important indicia of congressional intent that further support the view that a pledge of securities, which conveys legal rights in the securities for value, is a "sale" transaction within the statutory definition. The legislative history shows that Congress intended its definition of sale

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[35] Even a statement in the legislative history suggestive of a limited statutory purpose would not override express statutory language phrased in broad generic terms. See *Diamond* v. *Chakrabarty*, No. 79–136 (June 16, 1980), slip op. 12: "This Court frequently has observed that a statute is not to be confined to the 'particular application[s] . . . contemplated by the legislators.'"

to be a broad one. *United States* v. *Naftalin*, *supra*, 441 U.S. at 773; H.R. Rep. No. 85, 73d Cong., 1st Sess. 11 (1933). The legislative history also shows that Congress intended to pattern the definition of sale in the Securities Act of 1933 on an existing statutory precedent—the definition of "sale" contained in the Uniform Sale of Securities Act of 1929. As we demonstrate below, the Uniform Act included pledges within its definition of "sale." This review of the legislative history provides additional evidence that petitioner's narrow interpretation is at odds with the statutory design.[36]

1. Prior to the enactment of the Securities Act of 1933, 47 state legislatures had enacted their own securities laws, prescribing antifraud, registration and licensing provisions to regulate securities transactions. See S. Rep. No. 47, 73d Cong., 1st Sess. 2 (1933); *Federal Securities Act: Hearings on H.R. 4314 Before the House Comm. on In-*

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[36] Instead of analyzing the legislative history, petitioner relies (Br. 14, 15, 25) on a subsequent legislative event—the enactment of Section 2(a)(23) of the Public Utility Holding Company Act, 15 U.S.C. 79b(a)(23), in 1935. Section 2(a)(23) provides:

> "Sale" or "sell" includes any sale, disposition by lease, exchange or pledge, or other disposition.

This subsequent enactment does not affect the scope of the earlier statute, which includes in its generic definition of "sale" all dispositions of an "interest" in securities, including pledges. There is "no basis for reading into [Congress' later] actions an intent to modify the plain meaning of the words" used in the 1933 Act. *Diamond* v. *Chakrabarty*, *supra*, slip op. 10. As this Court emphasized in *United States* v. *Naftalin*, *supra*, 441 U.S. at 777 n.8, "subsequent enactments do not serve to restrict the original scope of § 17(a)." See also *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 197–200 (1963). Moreover, even if Section 2(a)(23) were relevant to the issue in this case, that provision clearly supports the government's position, not petitioner's position. The language used by Congress leaves no room to doubt that Congress believed that a "pledge" is a *type* of "disposition" of a security. And since *every* "disposition" of a security for value is covered by the definition of "sale" contained in the Securities Act of 1933, it follows plainly that the Securities Act's definition includes "pledges."

terstate and Foreign Commerce, 73d Cong., 1st Sess. 10 (1933) (hereinafter "*House Hearings*"); I L. Loss, *Securities Regulation*, *supra*, at 30–89. In light of the diversity of state statutes in this field, the National Conference of Commissioners on Uniform State Laws initiated a seven-year project in 1922 to draft a comprehensive "blue sky" law. See *Handbook and Proceedings*, *supra*, at 171 (1929). That project is of particular importance here because the culmination of the Commissioners' efforts—the Uniform Sale of Securities Act approved by the Conference of Commissioners and the American Bar Association in 1929—contained a definition of the term "sale" that Congress shortly thereafter incorporated almost verbatim in the Securities Act of 1933. See *House Hearings*, *supra*, at 13.

The first and second tentative drafts of the Uniform Sale of Securities Act defined the terms "sale" and "sell" to

> include the issuance of securities, an agreement whereby a person transfers or agrees to transfer an interest in securities, and an exchange, pledge, hypothecation, or any transfer in trust or otherwise by way of mortgage.

Handbook and Proceedings, *supra*, at 231 (First Draft) (1923); *id.* at 523 (Second Draft) (1924). The Commissioners apparently modeled this definition on the almost identical sale definition found in the Massachusetts blue sky law at that time. See 1921 Mass. Acts ch. 110 A, § 2(d), at 623. The same formulation was also adopted in other states. See, *e.g.*, California Corporate Securities Act, 1925 Cal. Stat. ch. 447, § 2(9), at 964–965; South Dakota Securities Law, 1927 S.D. Sess. Laws ch. 206, § 2(2), at 240.

Beginning with the third draft of the Uniform Sale of Securities Act prepared in 1927, this attempt to set forth a

particularized listing of specific types of sale transactions, such as issuance and pledges of securities, was abandoned in favor of a streamlined, generic definition. As finally adopted in 1929, the term "sale" was defined to "include every disposition, or attempt to dispose of a security or interest in a security for value." See *Handbook and Proceedings, supra,* at 174 (Fourth and Final Draft) (1929); *id.* at 578 (Third Draft) (1927).[37] At about this time, expansive sale definitions utilizing the "every disposition * * * of [an] interest in a security" phraseology began to appear in state blue sky laws. See, *e.g.*, Indiana Securities Law, 1925 Ind. Acts ch. 31, § 3(3), at 85; Illinois Securities Law, Ill. Ann. Stat. ch. 32, § 255, at 447 (Callaghan Supp. 1925–1931); Oregon Securities Law, 1929 Or. Laws ch. 461, § 6838(f), at 709–710; California Corporate Securities Act, 1929 Cal. Stat. ch. 707, § 2(a)(8), at 1252.

By including "every" disposition of an "interest in a security," these state laws and the Uniform Act embraced the full range of ownership interests and non-ownership interests in securities. The generic definition eliminated the need for a particularized listing of covered transactions. A listing of transactions would have been an invitation to evasion of the statutory purpose—to regulate the disposition for value of all legally recognized "interests" in securities.

Just one year before Congress enacted the Securities Act of 1933, the United States Court of Appeals for the Ninth Circuit considered the question whether a pledge of securities was a "sale" under the California Corporate Securities Act. *Cecil B. De Mille Productions, Inc.* v.

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[37] The Uniform Act further provided that: " 'Sale' or 'Sell' shall also include a contract to sell, an exchange, an attempt to sell, * * * a solicitation of a sale, * * * or an offer to sell * * *." *Handbook and Proceedings, supra,* at 174 (Fourth and Final Draft) (1929); *id.* at 578 (Third Draft) (1927).

Woolery, 61 F.2d 45 (9th Cir. 1932). As previously noted, California had followed the evolution of the Uniform Sale of Securities Act, first specifically defining the term "sale" to include pledges, and later adopting a generic definition extending to every disposition of an "interest" in a security for value. The Ninth Circuit stated in *Woolery* that the argument that a pledge was not a "sale" under the generic definition was "extremely specious," explaining (*id.* at 50; emphasis in original):

> As we have seen, the act defines "sale" as "every disposition, or attempt to dispose, of a security or *interest in a security* for value." Counsel * * * assert that "a pledgee has merely a special property or *interest in the thing pledged*." Therefore, it is obvious that, when the [pledgor] pledged these contracts for its debt to the [pledgee], the former "disposed" or attempted to dispose, of an "interest in a security."

2. The legislative history of the Securities Act of 1933 shows that Congress intended to incorporate the broad generic concept of sale evolved under the Uniform Sale of Securities Act of 1929. The draftsmen of the Securities Act borrowed heavily from state blue sky laws and, in particular, from the Uniform Sale of Securities Act of 1929. See *Aaron* v. *SEC*, *supra*, slip op. 8–9 (Blackmun, J., concurring and dissenting). As Huston Thompson, a principal draftsman of the federal legislation, observed:

> We had the Uniform Sale of Securities Act [before us]. It was drafted by the Commissioners of 38 States, I believe, in connection with the American Bar Association. We have followed the language in this bill wherever we could, and somewhat of its policy. That act, I may say, was worked out by lawyers and commissioners from the various States, and was then taken up before the American Bar Association. On two occasions the association has adopted and approved of it. So you see that we have a number of

> precedents here that have had approval by high authority.

House Hearings, supra, at 11. See also *Securities Act: Hearings on S. 875 Before the Senate Comm. on Banking and Currency,* 73d Cong., 1st Sess. 71 (1933).

The influence of the Uniform Act was nowhere more apparent than in the definitional provisions of the Securities Act of 1933. As Mr. Thompson stated, "[w]ith regard to the subject of definitions, I may say that we have attempted to follow the Uniform Sale of Securities Act * * *." *House Hearings, supra,* at 13. In fact, the definition of sale that Congress incorporated in the Securities Act of 1933 is virtually identical to the phraseology used in the Uniform Act. Compare Section 2(3) of the Securities Act of 1933, ch. 38, 48 Stat. 74 ("Sale" includes "every * * * disposition of * * * a security or interest in a security, for value"), with Section 1(3) of the Uniform Sale of Securities Act of 1929, reprinted in *Handbook and Proceedings, supra,* at 174 (Fourth and Final Draft) (1929) ("Sale" includes "every disposition * * * of a security or interest in a security for value"). Because Congress adopted the definitional language contained in the Uniform Act, and because that language embraced pledges, the term "sale" should extend to pledges in the present context. The Ninth Circuit's 1932 decision in *Woolery* authoritatively confirmed that the phraseology that Congress was soon to adopt included pledge transactions. The incorporated language should be given the same interpretation under the federal statute. See *Lorillard* v. *Pons,* 434 U.S. 575, 581 (1978): "where, as here, Congress adopts a new law incorporating sections of a prior law, Congress normally can be presumed to have had knowledge of the interpretation given to the incorporated law, at least insofar as it affects the new statute." See also *SEC* v. *Cap-*

ital Gains Research Bureau, Inc., 375 U.S. 180, 195 (1963).[38]

D. Fraud in the Pledge of Securities to a Bank Lender is the Type of Behavior That Congress Meant to Prohibit Under the Securities Act of 1933

Since the language used by Congress in defining the term sale "is sufficiently clear in its context" and is "not at odds with the legislative history," it is unnecessary to consider contentions bearing on the general "purpose" and "policy" of the Securities Act of 1933. *Aaron* v. *SEC*, *supra*, slip op. 14–15; *Ernst & Ernst* v. *Hochfelder*, *supra*, 425 U.S. at 214 n.33. Nonetheless, since petitioner bases his arguments in this Court in substantial part on what he terms "sound policy reasons" (Br. 20–26), we address these policy issues as well.

1. The Securities Act of 1933 was enacted by Congress in response to the stock market crash of 1929. *United States* v. *Naftalin*, *supra*, 441 U.S. at 775; *Ernst & Ernst* v. *Hochfelder*, *supra*, 425 U.S. at 194–195. The purpose of the Act was to "help set the economy on the road to recovery" during the depression (*United States* v. *Naftalin*, *supra*, 441 U.S. at 775) by "protect[ing] the investing

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[38] We acknowledge that it may not always be appropriate to assume that Congress intended to ratify prior judicial decisions construing state statutes used as models for federal legislation. See *Aaron* v. *SEC*, *supra*, slip op. 19 n.18. In *Aaron*, however, this Court concluded that the "state judicial interpretation" was "at odds with the plain meaning of the language Congress enacted * * *." *Ibid.* In contrast, the Ninth Circuit's *Woolery* decision is completely consistent with the plain meaning of the Securities Act's sale definition and is supported by the traditionally recognized principles of commercial law discussed on pages 25–29, *supra*. Thus, Congress' definition of the word "sale" comes "'freighted with the meaning imparted to [it] * * * by contemporaneous discussion. In such conditions, history is a teacher that is not to be ignored.'" *St. Paul Fire & Marine Ins. Co.* v. *Barry*, 438 U.S. 531, 545–546 (1978).

public and honest business * * *" (*ibid.*, quoting S. Rep. No. 47, 73d Cong., 1st Sess. 1 (1933)). Central to the economic difficulties that faced this nation following the market crash of 1929 was the failure of banks. Between 1921 and 1929, approximately 5,700 banks became insolvent, and the number of bank failures continued at an unprecedented pace during the depression.[39] For this reason, during the same year that Congress enacted the Securities Act of 1933, it also enacted the Banking Act of 1933, ch. 89, 48 Stat. 162 (the Glass-Steagall Act), which sought to prohibit federally insured banking institutions from engaging in certain securities activities deemed by Congress to be injurious. See *Investment Co. Institute* v. *Camp*, 401 U.S. 617, 629–634 (1971). Congress' concern for protection of the nation's banking institutions is also central to the federal securities laws. As Congress stated in Section 2 of the Securities Exchange Act of 1934, ch. 404, 48 Stat. 881, 15 U.S.C. 78b, federal "regulation and control" of securities transactions is essential "to protect and make more effective the national banking system and Federal Reserve System* * *." In particular, Congress declared that manipulation and control of securities prices is injurious to the national banking system because it tends to "prevent the fair valuation of collateral for bank loans and/or obstruct the effective operation of the national banking system and Federal Reserve System." *Ibid.*[40] This statement of regulatory purpose reflects Congress' awareness of the economic importance of the billions of

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[39] These bank failures are described in the legislative history of the Glass-Steagall Act, ch. 89, 48 Stat. 162. See S. Rep. No. 77, 73d Cong., 1st Sess. 8–10 (1933); 75 Cong. Rec. 9910 (1932) (remarks of Sen. Bulkley); see Lehr, *The Affiliation of Commercial Bank and Mutual Fund Personnel* (Pt.1), 83 Banking L.J. 377, 384 (1966).

[40] Petitioner's activities had precisely this effect. See pages 7–14, *supra*.

dollars of securities that are pledged as collateral with financial institutions in this country every year.[41]

Thus, it cannot seriously be contended that petitioner's fraud on Bankers Trust Company was beyond the concerns of the federal securities laws. To the contrary, petitioner's conduct is the very kind of conduct that Congress meant to prohibit when it outlawed fraud in every disposition of an interest in a security to protect investors, the general economy, and honest business. *United States* v. *Naftalin*, *supra*, 441 U.S. at 775–776.[42]

2. Petitioner nonetheless argues (Br. 20–23) that the Securities Act of 1933 is inapplicable here because the fraud that he practiced did not injure an "investor." That, however, is the same argument that this Court rejected in *United States* v. *Naftalin*, *supra*. In *Naftalin*, the defendant defrauded certain broker-dealers through a short selling scheme. The court of appeals held that the scheme was beyond the scope of the Securities Act because it had

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[41] The legislative history of this provision demonstrates Congress' concern over the impact of securities fraud on the operations of state and federal banks. See H.R. Rep. No. 1383, 73d Cong., 2d Sess. 4 (1934), noting that "[o]ver 13,000,000 men and women have savings accounts in mutual savings banks and at least 25,000,000 have deposits in national and State banks and trust companies—which are in turn large holders of corporate stocks and bonds." This Court has previously recognized that the antifraud provisions of the federal securities laws seek to protect creditors from fraud. See *Supt. of Insurance* v. *Bankers Life & Cas. Co.*, 404 U.S. 6, 12 n.8 (1971) ("Congress was especially concerned with the impact of frauds on creditors* * *").

[42] Rules of "lenity" and "strict construction" do not require a narrowing of the broad safeguards prescribed by Congress. See *United States* v. *Naftalin*, *supra*, 441 U.S. at 778–779; *SEC* v. *C.M. Joiner Leasing Corp.*, 320 U.S. 344, 354–355 (1943). Because the Securities Act of 1933 affords essential safeguards against fraud, it should be construed "not technically and restrictively, but flexibly to effectuate its remedial purposes." *SEC* v. *Capital Gains Research Bureau, Inc.*, *supra*, 375 U.S. at 195; *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972); *Tcherepnin* v. *Knight*, *supra*, 389 U.S. at 336.

no impact on investors, and merely injured financial intermediaries.[43] This Court rejected that contention, holding that the Securities Act was intended to protect "honest corporate business" as well as "investors." 441 U.S. at 775–776. The lower court decisions that petitioner cites (Br. 14–20), which have concluded that a "pledge" is not covered by the federal securities laws, rely on the same erroneous view of legislative intent. Thus, in *Lincoln National Bank* v. *Herber*, 604 F.2d 1038, 1041 (7th Cir. 1979) (emphasis in original), the court incorrectly reasoned that the securities laws were enacted solely "to protect the *investor*."[44] And in *National Bank of Commerce of Dallas* v. *All American Assurance Co.*, 583 F.2d 1295, 1300 (5th Cir. 1978), the court of appeals erroneously assumed that the federal securities acts are only "designed to protect investors. This purpose is not affected by a pledge of stock." In sum, the premise on which petitioner rests his principal policy argument—that Section 17(a) of the Securities Act of 1933 is inapplicable to fraudulent practices unless an investor is injured—has been authoritatively rejected by this Court's decision in the *Naftalin* case.[45]

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[43] The fraud in *Naftalin* is similar to the fraud practiced by petitioner. In *Naftalin*, the defendant falsely represented to the financial intermediary that he was the "owner" of the securities that he purported to convey. The false representations in both cases occurred in the process of disposing or attempting to dispose of a security or an interest in a security, and had serious economic consequences for the business firms that were victimized.

[44] *Herber* applied this view of legislative intent instead of the plain meaning of the statute. The court recognized that the "sale" definition prescribed by Congress "would appear broad enough to embrace a transfer of a security interest in stock." 604 F.2d at 1040.

[45] The Second and Sixth Circuits have rejected petitioner's policy argument by holding that the antifraud provisions of the federal securities laws afford protection against fraud in the pledge of securities. *United States* v. *Gentile*, *supra*, 530 F.2d at 466–467 (Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a)); *Mallis* v. *FDIC*, 568 F.2d 824, 828–830 (2d Cir. 1977), cert. dismissed, 435 U.S. 381 (1978)

Moreover, as this Court emphasized in *Naftalin*, "the welfare of investors and financial intermediaries are inextricably linked—frauds perpetrated upon either business or investors can redound to the detriment of the other and to the economy as a whole." 441 U.S. at 776. Thus, while individual investors may suffer "no immediate financial injury" when a bank is defrauded in the pledge of securities (*ibid.*), such investors often prove to be the ultimate victims of fraudulent pledge transactions. If a pledgor fails to repay the loan, the pledgee, in reselling the collateral upon default, may serve as a conduit through which uninformed public investors who purchase the pledged securities are defrauded. Such investors often purchase counterfeit securities, worthless securities, or stolen securities that have been pledged through fraudulent schemes of the kind practiced by petitioner. See *Organized Crime—Stolen Securities: Hearings Before the Permanent Subcomm. on Investigations of the Senate Comm. on Government Operations*, 92d Cong., 1st Sess. 746–747 (1971); *Organized Crime—Securities: Thefts and Frauds: Hearings Before the Permanent Subcomm. on Investigations of the Senate Comm. on Government Operations*, 93d Cong., 1st Sess. 75–76 (1973).[46]

(per curiam), on remand, 615 F.2d 68, 74–75 (1980), petition for cert. pending, No. 79–1426 (filed Mar. 14, 1980) (Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b)); *Mansbach* v. *Prescott, Ball & Turben*, *supra*, 598 F.2d at 1027–1028 (Section 10(b) of the Securities Exchange Act of 1934). See also *Kerbs* v. *Fall River Industries, Inc.*, *supra*, 502 F.2d at 739.

[46] It is, of course, irrelevant that petitioner's fraudulent pledges took place in "face to face" transactions rather than "in the organized markets." *Supt. of Insurance* v. *Bankers Life & Cas. Co.*, *supra*, 404 U.S. at 12. It is also irrelevant that the immediate victim was a "sophisticated" bank (Bossier Amicus Br. 5). As the Fifth Circuit noted in *Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville*, 409 F.2d 989, 992 (5th Cir. 1969), "[f]raud may be * * * perpetrated upon the powerful and the sophisticated," as well as the "unsophisticated and the unwary * * *."

3. In a related argument (Br. 22), petitioner contends that the "risk" that the victim of his fraud assumed was commercial in nature, and that this should bar his prosecution under the Securities Act of 1933. However, there is nothing in the statute that suggests that the nature of the "risk" assumed by the victim of the fraud has any significance. Here, as in *United States* v. *Culbert*, *supra*, 435 U.S. at 380, the Court should decline petitioner's invitation to "limit the statute's scope" by reference to "undefined categor[ies]" such as commercial risk and investment risk.[47] Congress has drafted the statute unambiguously to apply to "every" disposition of an "interest" in a security for value. It makes no difference whether the disposition occurs in a "commercial" or "investment" setting. That is, the victim of the scheme may be either an "investor" or a "financial intermediary" as in *Naftalin*. If the definition prescribed by Congress is satisfied, the statute applies; "'[n]othing on the face of the statute suggests a congressional intent to limit its coverage'" to particular categories of arbitrarily defined risks. 441 U.S. at 774 n.5.[48] Thus,

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[47] Of course, the scheme in *United States* v. *Naftalin*, *supra*, which this Court determined was in violation of Section 17(a), did not involve a victim who assumed an "investment risk." Instead, the defrauded financial intermediary assumed a commercial risk inherent in delivering securities to other persons. See also *United States* v. *Brown*, 555 F.2d 336, 338–339 (2d Cir. 1977), cited with approval in *Naftalin* (441 U.S. at 775), where the defrauded victim assumed a commercial risk inherent in its role as a transfer agent, not an investment risk.

[48] An attempt to narrow the coverage of the Act's definition of "sale" by reference to undefined categories such as "commercial risk" and "investment risk" could lead to substantial ambiguities and arbitrary reductions in the protection that it affords. Various securities transactions entered into by financial institutions could arguably be characterized as "commercial" in nature. For example, a bank trust department may purchase equity securities for investment (generally in a privately negotiated transaction) under an agreement giving it the option to resell the securities to the seller at a later date. It could be argued that such a transaction is similar to an extension of credit se-

although petitioner urges the Court to look to "economic realities" (Br. 19), the "reality" of the transaction that he engaged in is a disposition of an interest in securities for value—precisely the kind of transaction that Congress meant to protect from fraud.

The commercial/investment dichotomy that petitioner would apply has been used by some lower courts in determining whether promissory notes or similar instruments are "securities" within the meaning of the federal securities laws. See, *e.g.*, *Sanders* v. *John Nuveen & Co.*, 463 F.2d 1075, 1079–1080 (7th Cir.), cert. denied, 409 U.S. 1009 (1972). Here, however, there is no doubt that the instruments that petitioner pledged were securities, and the dichotomy that petitioner suggests is not useful in determining whether an "interest" in those securities was disposed of for value.[49]

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cured by stock, that the context is thus "commercial," and that the antifraud provisions of the federal securities laws therefore do not apply. Such an interpretation, however, would diminish the safety of the nation's financial institutions and conflict with the unambiguous prohibition of fraud in every disposition of a security or interest in a security for value.

[49] The reliance of petitioner and amicus on *International Brotherhood of Teamsters* v. *Daniel*, *supra*, and *United Housing Foundation, Inc.* v. *Forman*, 421 U.S. 837 (1975), is entirely misplaced. In those cases, the Court applied the "economic realities" test in construing the definitions of the term "security" under the federal securities laws. In *Daniel*, the question before the Court was whether a participation in an involuntary noncontributory pension plan was an "investment contract" and therefore was within the definitions of "security" in the Securities Act of 1933 and the Securities Exchange Act of 1934. The Court applied the test prescribed in prior cases ("the 'touchstone' of the * * * test 'is the presence of an investment in a common enterprise premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others'") to answer that question (439 U.S. at 561). In *Forman*, the Court held that shares in a state-subsidized housing cooperative were neither "stock" nor "investment contracts" and thus were not "securities." In reaching its decision, the Court relied on legislative history indicating that Congress intended the definition of "security" to include the "many types of instruments that in our

Moreover, petitioner's suggested dichotomy between investors and pledgees, and the risks assumed by them, is an artificial one. As the Second Circuit pointed out in *United States* v. *Gentile*, *supra*, 530 F.2d at 467, a commercial bank that parts with substantial sums of money on the understanding that valuable securities are being conveyed to it to secure its claims assumes a risk like that of an investor:

> [T]he pledgee assumes a very real investment risk that the pledged securities will have continuing value, a risk that is identical in nature to the risk taken by investors which serves as the indisputable basis for statutory regulation of securities transactions.

In determining whether to approve a request for a secured loan, banks rely on the investment quality of the collateral (see pages 4–14, *supra*). When securities are pledged as collateral, the valuation process is much the same as if the creditor were purchasing them outright. Factors such as the grade, price, price stability, yield, degree of marketability, and diversification are all considered. The emphasis on value is further reflected in the common provision in secured loan agreements requiring that a minimum ratio of the current market value of the pledged securities to the amount of the outstanding loan be maintained. See generally, K. Lott and R. Myers, *Secured Lending*, *reprinted in* W. Baughn and C. Walker, *The Bankers Handbook* 641–643 (rev. ed. 1978).[50]

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commercial world fall within the ordinary concept of a security." 421 U.S. at 847–848, quoting H.R. Rep. No. 85, 73d Cong., 1st Sess. 11 (1933). The Court concluded that the purchase of "subsidized low-cost living space" (421 U.S. at 851) did not meet that test. In discussing the definition of "security," neither *Forman* nor *Daniel* shed light on the unrelated question of statutory interpretation presented here.

[50] Bankers accepting securities as collateral look to "credit quality, marketability and price volatility properties." Unlisted stocks and stocks that have a "limited market" are substantially less attractive to

While it is true, as petitioner contends (Br. 19), that banks obtain collateral on the understanding that it will be disposed of only in the event of a default, the prospect of a default is an ever-present danger that the collateral protects against. Where, as here, the bank is willing to part with its money only if the borrower assigns high quality and fully marketable securities, it is clear that a central element in the bank's decision to put its capital at risk, and an essential element of its bargain, is the "disposition" of an "interest" in the securities. As in the case of a purchaser in an ordinary securities transaction, the pledgee is vulnerable to fraud and stands to lose its assets if the securities prove worthless. Misrepresentations concerning the value of the securities deprive a pledgee, like any other purchaser, of its bargained-for valuable "interest" in the securities.[51]

4. Finally, petitioner contends that there is no need to provide a federal "remedy" in cases such as this because

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bankers than marketable securities issued by high quality companies. D. Hayes, *Bank Lending Policies* 164–167 (2d ed. 1977). See also H. Prochnow and R. Foulke, *Practical Bank Credit* 339 (2d ed. 1963), explaining that "a banker should generally obtain as collateral not only listed securities but also those in which trading is active. * * * [W]henever possible, the securities should represent well-established corporations, ably managed, and with a steady record of earnings." Accord, I M. Corns, *The Practical Operations and Management of a Bank* 449 (1962). See also American Bankers Association, Commercial Lending Division, *A Guide To Developing A Written Lending Policy* 17 (1977), noting that stock issued by a corporation "having no ready market value" is unacceptable as collateral. When reliable market values are not readily ascertainable, the bank accepting collateral should obtain "the latest financial statement of the corporation" to be "analyzed" so that "the book value [can be] obtained." M. Groves, *Loan Review: A Guide* 20–21 (1978). In sum, a bank parting with its money in reliance on collateral to secure its loan analyzes the securities that it receives in a manner similar to that of an ordinary conservative investor.

[51] It is ironic for petitioner to argue (Br. 19) that the bank's partial reliance on the assets and earning power of Tri-State as a source for

defrauded pledgees already have an adequate remedy "on a promissory note against the maker and any guarantor," that application of the federal securities laws is "unnecessary" because other federal antifraud statutes are applicable, and that fraudulent pledges are a matter of primary concern to the states rather than the federal government (Br. 10–11, 15, 25–26). There is no merit to any of these contentions.

a. At the outset, we emphasize that there is no question in this case of affording private remedies, express or implied. This case involves a criminal prosecution expressly authorized by Congress under 15 U.S.C. 77x. See *United States* v. *Naftalin*, *supra*, 441 U.S. at 774 n.6. This Court need not decide whether a violation of Section 17(a) of the Securities Act of 1933 gives rise to a private right of action in favor of any person. See *Aaron* v. *SEC*, *supra*, slip op. 8; *Blue Chip Stamps* v. *Manor Drug Stores*, *supra*, 421 U.S. at 733–734 n.6. Nor should this Court decline to enforce the criminal penalties prescribed by Congress simply because, as petitioner asserts, a bank creditor has a civil contract remedy against its borrowers. In this case, that civil remedy was wholly non-existent because the collateral was virtually worthless, the borrower was insolvent, and petitioner (who had guaranteed repayment of the loan) filed a bankruptcy petition (see page 14, *supra*). Crimi-

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repayment of its loans should strip the bank of protection against fraud in the pledge of securities. Petitioner repeatedly deceived the bank into believing that Tri-State had substantial assets and earning power, and thereby diverted the bank from a careful check on the value of the collateral (see pages 3–6, *supra*). Of course, petitioner's fraudulent practices also prevented the bank from analyzing the value of the collateral when it sought to do so (see pages 9, 11, *supra*). Finally, petitioner's argument overlooks the fact that the very purpose of a security interest in marketable stock collateral is to enable the lender to obtain repayment of its loan in the event of default without having to look to the borrower's other assets. See *United States* v. *Gentile*, *supra*, 530 F.2d at 467.

nal sanctions are essential to deter other persons from engaging in such egregious fraudulent schemes.[52]

b. Application of Section 17(a) to petitioner's fraudulent scheme is unaffected by the fact that other federal criminal statutes also apply. Section 17(a) complements the protections afforded by other federal criminal statutes. As Senator Fletcher explained during the floor debates on the Securities Act of 1933 (77 Cong. Rec. 2983-2984 (1933)):

> Under the provisions of the bill we do not in anywise restrict or limit or weaken the laws already on the statute books. We are trying to cover instances where there seem to be loopholes and means of escape, and to apply the measure particularly to the matter of dealing in securities. * * * The bill rather strengthens and broadens the authority to proceed in such instances.

Moreover, as this Court repeatedly has recognized in securities fraud cases, statutory overlap with other antifraud provisions is neither unusual nor unfortunate. See *Edwards* v. *United States*, 312 U.S. 473, 484 (1941) ("[t]he two [antifraud statutes] can exist and be useful, side by side"); *United States* v. *Naftalin*, *supra*, 441 U.S. at 777-778 ("[the defendant] is undoubtedly correct that the two Acts prohibit some of the same conduct. * * * [But

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[52] Amicus Bossier Bank argues (Br. 5) that application of Section 17(a) to pledge transactions would require pledgors to furnish disclosure statements equivalent to registration statements. However, registration statements are required under the Securities Act of 1933 when securities are offered to the public by issuers, underwriters or control persons. They are not required in ordinary transactions in the aftermarket when unrestricted securities are traded or pledged by persons not affiliated with the issuer. See Section 4(1) of the Act, 15 U.S.C. 77d(1). Of course, the general antifraud provisions of the federal securities laws forbid deceptive statements and concealment of material information needed to avoid deception when securities are traded or pledged. These, however, are simply prohibitions of fraudulent conduct. We also note that a pledgor would be subject to criminal prosecution under Section 17(a) only if he engaged in deceptive practices "willfully." 15 U.S.C. 77x.

that] certainly does not absolve [him] of guilt for the transactions which violated the statute under which he was convicted."); *SEC* v. *National Securities, Inc.*, *supra*, 393 U.S. at 468 ("The fact that there may well be some overlap is neither unusual nor unfortunate."); see generally *United States* v. *Batchelder*, 442 U.S. 114, 123-124 (1979).[53]

c. Petitioner's contention that fraudulent pledges are of concern only to the states, and not the federal government, is refuted by the legislative history of the Securities Acts Amendments of 1975, Pub. L. No. 94-29, 89 Stat. 97. Prior to the enactment of that legislation, Congress held a series of hearings focusing on the involvement of organized crime in the securities field.[54] Those hearings

[53] Even though other federal antifraud statutes can often be relied on by the government in criminal cases, Section 17(a) serves an essential complementary purpose because it can be enforced by the Securities and Exchange Commission in civil injunctive proceedings brought to prevent injury caused by fraudulent pledge transactions. See *Aaron* v. *SEC*, *supra*. The SEC can sue in federal court to obtain injunctive and ancillary relief and can also institute disciplinary proceedings against securities industry professionals who violate Section 17(a). See, *e.g.*, Section 20(b) of the Securities Act of 1933, 15 U.S.C. 77t(b); Section 15 of the Securities Exchange Act of 1934, 15 U.S.C. 78*o*. In addition, other potentially applicable statutes prescribed by Congress have different coverages. For instance, 18 U.S.C. 1014, cited by petitioner (Br. 25), extends only to specified financial institutions and would not, standing by itself, prevent fraudulent pledges to other institutions such as insurance companies or brokerage houses.

[54] See *Organized Crime—Stolen Securities: Hearings Before the Permanent Subcomm. on Investigations of the Senate Comm. on Government Operations*, 92d Cong., 1st Sess. (1971) (hereinafter "*Hearings on Stolen Securities*"); Organized Crime—*Securities: Thefts and Frauds: Hearings Before the Permanent Subcomm. on Investigations of the Senate Comm. on Government Operations*, 93d Cong., 1st Sess. (1973) (hereinafter "*Hearings on Thefts and Frauds*"); Organized Crime—*Techniques for Converting Worthless Securities Into Cash: Hearings Before the House Select Comm. on Crime*, 92d Cong., 1st Sess. (1971) (hereinafter "*Hearings on Techniques for Converting Worthless Securities Into Cash*"); see also 121 Cong. Rec. 10733 (1975) (remarks of Sen. Jackson).

show beyond question that organized crime has disposed of massive quantities of stolen, counterfeit and worthless securities by fraudulently pledging them to banks as collateral for loans. Pledging securities as collateral for loans is a primary means by which worthless, counterfeit, and stolen securities are converted into cash, often for reinvestment into organized crime activities. The total value of lost and stolen securities was estimated to be as high as $50 billion.[55]

Far from being an issue of merely local significance, these congressional hearings reveal that organized crime engages in fraudulent pledge transactions on a nationwide basis, and often on an international basis. Federal law enforcement resources are essential in combatting securities fraud occurring on this scale. As Senator Jackson noted at the commencement of the *Hearings on Thefts and Frauds*, "stolen, counterfeit, and worthless securities" are used as "a basis for worldwide swindles cloaked in legitimacy, made even more dangerous by the extensive involvement of organized criminal groups." *Id.* at 1; see also *id.* at 2-5, 42-43, 124, 285, 479-482. He emphasized that "[t]his problem goes to the very foundation of our financial system." *Id.* at 2. The hearings focus repeatedly on the use of "phony loan schemes perpetrated via stolen and counterfeit securities * * *." *Id.* at 4; see *id.* at 75-76, 104, 130-131, 187, 316, 391, 406, 456, 518-519, 566 (pledge of stolen or counterfeit securities); see also *id.* at 263-264, 390, 454, 482 ("rental" of worthless securities to defraud bank lenders). In light of these revelations, Senator Jackson concluded that "[t]he situation is both serious and dangerous and strong Federal action is warranted," adding that "some observers feel that the integrity of the entire financial community is at stake." *Id.* at 480-481.

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[55] *Hearings on Thefts and Frauds, supra*, at 5, 20, 57.

The *Hearings on Stolen Securities* tell a similar story. As Senator McClellan pointed out (*id.* at 10):

> A variety of means are used to market stolen securities. The most common is the direct sale through brokerage houses and banks. However, a safer means from the viewpoint of the criminal is to pledge the securities as collateral for loans from banks and finance companies. Stolen securities can also be "rented" by a loan shark to a business man in need of loans. He, in turn, either pledges the securities as collateral for loans or adds them to otherwise legitimate balance sheets for the purpose of enhancing his credit rating.

These hearings are replete with descriptions of fraudulent pledges by organized crime of worthless, stolen and counterfeit securities as collateral for loans. *Id.* at 2, 9, 25, 39–41, 44, 48, 64, 73–75, 98, 283, 675, 676–678, 698, 745, 746–748, 847–856, 876, 894–897, 959–960, 1117–1118. Senator McClellan observed that "we have every reason to believe that the illicit traffic of negotiable securities is the latest and one of the most lucrative areas of concentration for most organized mobs in this country." *Id.* at 4. Corrective action in this field is the responsibility of both federal and local prosecutors, who have "concurrent jurisdiction," as the Attorney General explained. *Id.* at 27.

During the *Hearings on Techniques for Converting Worthless Securities Into Cash*, Congressman Pepper emphasized that local law enforcement efforts are insufficient to stop organized crime from defrauding financial institutions (*id.* at 1–2):

> Our investigation discloses that there is a national apparatus of individuals who are continually engaged in organized criminal conduct directly concerned with commercial transactions. * * * The essence of their activity is to give worthless securities, or commercial paper, a facade of value and respectability and then

> convert the worthless paper into hard cash. * * * These individuals move across state lines—from coast to coast and internationally—bankrupting small banks, insurance companies, and stock brokerage institutions. Local law enforcement is entirely inadequate to cope with a scheme which is planned in California, prepared in New Jersey, and executed in Ohio.

Congressman Pepper also noted (*id.* at 3):

> A * * * device currently used by sophisticated organized criminal elements is the bank loan which is secured by worthless securities. Our investigation demonstrated that numerous banks throughout the country were defrauded when they issued loans which were secured by worthless * * * notes. One bank in Ohio was nearly bankrupted when it suffered losses of over $1 million.

See *id.* at 242, 259, 268, 306, 308, 361, for a description of the techniques organized crime employs in obtaining bank loans through fraudulent pledges.[56] At the conclusion of these hearings, Congressman Pepper admonished that organized crime had defrauded banks and other financial institutions of "millions of dollars annually" and that "more aggressive procedures on the part of governmental entities which are responsible are absolutely necessary." *Id.* at 361.[57]

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[56] The extensive involvement of organized crime in fraudulent pledge transactions is also recounted in Note, *Insecure Securities: Thefts of Stocks and Bonds*, 6 Colum. J. L. & Soc. Prob. 478, 483-484 (1970); Koblenz, Weglian, Kieszkiel, and Dawson, *Let's Blow the Whistle on the Securities Game*, 60 A.B.A. J. 461-463 (1974).

[57] The facts disclosed in the foregoing hearings prompted Congress to add Section 17(f)(1), 15 U.S.C. 78q(f)(1), to the Securities Exchange Act of 1934 in 1975. See 89 Stat. 137. Under that provision, federally insured banks, among others, are required to report information about missing, counterfeit and stolen securities to the Securities and Exchange Commission pursuant to Commission rules. Under this statutory authority, the Commission has established a lost and stolen secu-

In sum, there is no merit to petitioner's assertion that fraudulent pledges are a matter of merely local concern. The legislative history of the Securities Acts Amendments of 1975 shows beyond genuine doubt that fraudulent pledges pose a serious threat to both the nation's financial institutions and financial markets, national assets that it was the purpose of the federal securities laws to preserve.[58]

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rities program that includes bank pledgees. See 17 C.F.R. 240.17f-1. As of December 1979, the Commission had compiled a computerized data base covering over $2 billion in lost, counterfeit, and stolen securities. See SEC Staff Report, *Lost and Stolen Securities Program, 1979 Statistics*. Congress' enactment of Section 17(f)(1) is but a further reflection of its determination that federal action is essential to prevent fraud in the pledge of securities.

[58] Petitioner cites Professor Loss' treatise (I *Securities Regulation* 649 (2d ed. 1961)) for the proposition that enactment of the Securities Act of 1933 was not "needed" to reach fraudulent pledges. Petitioner fails to note that Professor Loss explicitly recognizes that "[i]t is probably easier under the language of § 2(3)—'every * * * disposition of a security, or interest in a security, for value'—to say that a pledge involves a 'sale' than that it does not. Hence every pledgee may be considered to be a person who 'purchases' within the meaning of § 2(11)." Professor Loss explains that this analysis is relevant in deciding whether "a fraudulent pledgor violates § 17(a)." *Ibid.* Professor Loss' remark in 1961 on the "necessity" of enacting federal legislation in this field was a preface to his discussion of the question, not involved in this case, whether a pledgee who receives securities from an issuer, underwriter, or control person is required to obtain a registration of the securities before selling them to the public. See also Sargent, *Pledges and Foreclosure Rights Under the Securities Act of 1933*, 45 Va. L. Rev. 885, 893-894 (1959).

Professor Loss is currently the reporter for the proposed *Federal Securities Code* (Proposed Official Draft 1980). The Code, which has been approved by the American Bar Association and the American Law Institute, expressly "define[s] a pledge as a sale for purposes of the fraud part." ALI *Federal Securities Code*, Comment (6) to § 202(143), at 190 (1980); see *id.* at § 202(143)(F) ("The terms [sale, sell, offer and offer to sell] * * * include * * * for purposes of part XVI ["fraud, misrepresentation, and manipulation"], a hypothecation or security loan").

CONCLUSION

The decision of the court of appeals should be affirmed.

Respectfully submitted.

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No. 79-1013

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

WILLIAM RUBIN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR BOSSIER BANK & TRUST COMPANY AS AMICUS CURIAE

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INTEREST OF AMICUS CURIAE

Bossier Bank & Trust Company ("BBT") is a Louisiana banking corporation whose business is regulated and supervised by the Louisiana State Banking Department and the Federal Deposit Insurance Corporation. BBT is interested in the present case because this Court's opinion may affect *First National Bank of Las Vegas, New Mexico* v. *Estate of Milton B. Russell, et al.*, No. 80-1401 in the United States Court of Appeals for the Fifth Circuit, in which BBT is an appellee. *First National Bank* is an appeal from the order of the United States District Court for the Southern District of Texas granting summary judgment for BBT and the other defendants in a private action for damages brought by First National Bank of Las Vegas. The district judge determined that a repurchase transaction involving fictitious United States treasury notes did not constitute a purchase or sale of a security for purposes of § 10(b) of the Securities Exchange Act of 1934. BBT will support the district court's judgment on appeal by contending that the transaction in question was essentially a loan in which the treasury notes were to be pledged as collateral. Therefore, BBT supports petitioner's argument in the present case that a pledge of securities is not a "sale" for purposes of the federal securities laws.

SUMMARY OF ARGUMENT

The Court should construe the term "sale" in light of the purposes of the antifraud provisions of the federal securities laws. Neither the language nor the legislative history of these statutes provides any indication that Congress intended to bring within their scope the pledging of securities as collateral for commercial loans. There is no significant public policy that would be served by extending the protection of federal securities laws to secured lenders in this context.

The Court should not rely upon the passage of "title" for determining whether there has been a sale of securities that are pledged as collateral for a loan. Instead, a test of economic reality should be employed for determining whether a transaction is essentially a transfer of ownership or a secured loan.

ARGUMENT

(1) The Court Should Adopt the Position of the Fifth and Seventh Circuits and Hold that a Pledge of Securities as Collateral for a Loan Is Not a "Sale" for Purposes of the Antifraud Provisions of the Federal Securities Laws.

The question in the present case is whether the pledge of securities as collateral for a loan is a "sale" within the meaning of § 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a). But the resolution of this question will undoubtedly affect the interpretation of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5. The courts of appeals have uniformly held that the definitions of "sale" and "purchase or sale" in the antifraud provisions of these two acts should be given the same interpretation with regard to pledges. *Lincoln National Bank* v. *Herber,* 604 F.2d 1038, 1040-41 (7th Cir. 1979); *Mansbach* v. *Prescott, Ball & Turben,* 598 F.2d 1017, 1028-29 (6th Cir. 1979); *National Bank of Commerce* v. *All American Assurance Co.,* 583 F.2d 1295, 1298 (5th Cir. 1978); *Mallis* v. *FDIC,* 568 F.2d 824, 829-30 (2d Cir. 1977), *cert. dismissed,* 435 U.S. 388 (1978).

In this context, the Solicitor General's argument based on the literal definition of "sale" in the 1933 Act, 15 U.S.C. § 77b(3), is disingenuous. *See* Brief for the United States on Petition for Certiorari, at 9. It is true that the statutory

definition includes every "disposition of a security or interest in a security" and that a pledge could be described as creating an "interest" in a security even though it does not transfer ownership. But the opposite conclusion would have to be drawn from the literal definition of "sale" in the 1934 Act, 15 U.S.C. § 78c(a)(14), which includes only a "contract to sell or otherwise dispose of" a security, and makes no mention of the transfer of a mere "interest" in a security. In summary, the word "interest" in the definition of "sale" in the 1933 Act cannot be given controlling significance unless the Court is prepared to treat pledge transactions differently under the 1934 Act.[1]

The legislative histories of the definitions of the terms "sale" and "purchase or sale" in the two acts contain no evidence of an intention to include pledge transactions. *See* J. ELLENBERGER & E. MAHAR, LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934, vol. 1, p. xix & vol. 4, p. xv (1973). In 1935, only one year after the enactment of the Securities Exchange Act, Congress specifically listed pledges within the definition of "sale" in the Public Utility Holding Company Act, 15 U.S.C. § 79b(23). Thus it appears that Congress was well aware of the practice of pledging securities at the time it drafted the 1933 and 1934 acts and simply did not include such pledges within the definition of a "sale" for purposes of those acts.

A common sense approach based on the purposes of the two acts supports the view that they were not intended to cover pledge transactions. The evils toward which these acts were directed are not involved where securities are used as collateral for a loan. The practices toward which the legislation was aimed involved the issuance of worthless

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[1] For an argument that the 1934 Act imposes less liability for pledge transactions than the 1933 Act, see Note, *A Pledge of Stock in a Commercial Loan: "Purchase or Sale" under the Securities Exchange Act of 1934?*, 1979 ARIZ. ST. L.J. 669, 675-77.

new securities and transactions designed to influence the price at which securities sold in subsequent markets by affecting (or appearing to affect) the forces of supply and demand.[2] A pledge of securities, however, is a non-market transaction which has no effect upon the market price of securities. The pledge of securities as collateral for a loan primarily affects the market for loanable funds, a market that the drafters of the 1933 and 1934 acts did not purport to regulate except for changes in margin requirements.

Moreover, it is unnecessary to give the federal securities laws an expansive interpretation to provide secured lenders with protection against fraud. A secured lender, unlike the the outright purchaser or seller of securities, always has a right of action on the debt itself. State laws, including the Uniform Commercial Code, extensively regulate secured transactions and the remedies for default. *See Lincoln National Bank* v. *Herber,* 604 F.2d 1038, 1044 (7th Cir. 1979). Federal law also provides criminal sanctions for making false statements to most financial institutions in connection with applications for loans or pertaining to the security therefor. 18 U.S.C. § 1014.[3] In summary, secured

[2] The 1933 Act was designed to protect the investor in securities. *See* S. Rep. No. 47, 73rd Cong., 1st Sess. (1933); H.R. Rep. No. 85, 73rd Cong., 1st Sess. (1933); 77 Cong. Rec. 2983 (1933) (remark of Sen. Fletcher). The 1934 Act was designed to remedy several perceived problems and manipulative practices, including (1) the manipulation of the securities market by members of the securities exchanges, (2) naked speculation encouraged by low margin requirements, and (3) the exploitation of uninformed investors by the use of speculative pools, wash sales and matched orders, and other devices. Message from the President – Regulation at Securities Exchanges, S. Doc. No. 132, 73rd Cong., 2nd Sess. (1934); 78 Cong. Rec. 7690 (1934) (remarks of Rep. Cooper); H.R. Rep. No. 1383, 73rd Cong., 2d Sess. 2-5, *contained in,* 78 Cong. Rec. 7702-03 (1934).

[3] The statute provides criminal penalties for one who "knowingly makes any false statement . . . for the purpose of influencing in any way the action of," *inter alia,* a federally-insured financial institution, "upon any loan . . . or the acceptance, release or substitution of security therefor . . . ." 18 U.S.C. § 1014.

lenders are well protected without coverage by the federal securities laws.

Applying the antifraud provisions of the securities laws to the pledge of securities as collateral for commercial loans could also have far-reaching consequences on the credit markets. Corporate finance transactions involving a pledge of securities would probably have to include extensive disclosures similar to those required for the registration of an issuance of those securities.[4] The requirement of such disclosure statements would increase the cost of commercial borrowing and serve no useful purpose. A commercial lender is generally sophisticated and can always require, as a prerequisite to granting a loan, such disclosures as it believes would be useful. The effect of extending securities law coverage to this situation would be to require additional disclosures that lenders do not want and borrowers should not have to pay for.

(2) The Court Should Employ a Test of "Economic Reality" for Determining When a Transaction is a Secured Loan Rather than a Sale of Securities.

The first point of this brief argues that the pledge of securities as collateral for a loan should not be regarded as a sale for purposes of the antifraud provisions of federal securities law. Amicus curiae suggests further that economic reality rather than technical notions of "title" should govern application of this holding if adopted by the Court.

It is a commonplace that substance rather than form should control the application of the antifraud provisions of the federal securities laws. *United Housing Foundation* v. *Forman,* 421 U.S. 837, 849 (1975); *Tcherepnin* v. *Knight,*

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[4] As this Court well knows, cautious participants in securities transactions make exhaustive disclosures to avoid subsequent litigation based on the theory that there was a failure to disclose some material fact.

389 U.S. 332, 336 (1967). In this regard, for example, a transaction that has the effect of a sale of securities should be treated as a sale, even though it is pretextually structured as a pledge. *Herpich* v. *Wallace* 430 F.2d 792, 810-11 (5th Cir. 1970); *see National Bank of Commerce* v. *All American Assurance Co.,* 583 F.2d 1295, 1300 (5th Cir. 1978).

On the other hand, a pledge of securities should not be retroactively transformed into a sale just because of a subsequent default in the loan. *But cf. McClure* v. *First National Bank,* 497 F.2d 490, 495-96 (5th Cir. 1974), *cert. denied,* 420 U.S. 930 (1975), *criticized in United States* v. *Gentile,* 530 F.2d 461, 467 n.6 (2d Cir.), *cert. denied,* 426 U.S. 936 (1976). As a practical matter, such a holding would largely negate the benefits of the rule advocated in part one of this brief. A secured creditor is most likely to allege securities fraud when the debtor has defaulted. If the creditor could then retroactively transform the pledge into a sale by foreclosing, securities law coverage could be easily obtained in most cases.[5] A better approach would be to hold that the transaction is characterized as a pledge or sale on the basis of its structure at the time it is entered into.

Another potential pitfall associated with undue reliance upon the concept of "title" involves the interplay of federal securities law and the state law of secured transactions. No useful purpose would be served by requiring in each

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[5] Of course, the foreclosure sale of the securities by the pledgee could itself be a "sale" to which the federal securities laws apply. *See* SEC v. Guild Films Co., 279 F.2d 485 (2d Cir.), *cert. denied,* 364 U.S. 819 (1960). Amicus curiae does not support this rule, since it imposes severe burdens on foreclosing lenders when the collateral consists of unregistered securities. But, in any event, a subsequent foreclosure sale should not be held retroactively to transform the original secured loan transaction into a "sale" as well.

case an inquiry into the metaphysics of "title" or its passage under the applicable state laws. Such an approach would create a potential for inconsistent applications of federal law, depending upon the way the transaction in question is treated under the law of the various states.[6] State law on secured transactions involving securities is very complex.[7] The Court risks unintended consequences if it adopts a mechanical rule for determining when a pledge of securities must be regarded as a "sale." A better approach would be to hold simply that a transaction which in substance involves the use of securities as collateral for

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[6] The laws of the various states are not uniform on the subject of secured interests in securities. In most states, the law concerning this subject is based on Article 9 of the Uniform Commercial Code. The common law "pledge" is perpetuated in Section 9-305, which provides for the perfection of a security interest by the possession of certain kinds of collateral, subject to the exceptions for nonpossessory perfection in section 9-304(4) & (5).

In 1977, however, Articles 8 and 9 were revised, and a few states have adopted these revisions. A major reason for the 1977 revision was to create a body of law to govern uncertificated securities. A new section 8-321 was added to govern the creation, perfection, and termination of security interests in all securities, both certificated and uncertificated. For uncertificated securities a new mechanism, "registration of pledge," was created in section 8-108 for evidencing a security interest, as an alternative to the more conventional procedure of registering a transfer to the secured party.

Finally, paragraph 3 of the official comment to section 8-102 makes clear that the definition of a "security" for purposes of the UCC is not coextensive with the definitions of this term in the federal securities laws. The creation of security interest in unconventional securities would thus continue to be governed by Article 9 or pre-Code law even in those states that have adopted the 1977 revisions.

For a discussion of some choice of law problems created by the old and new version of Articles 8 and 9, see R. WEINTRAUB, COMMENTARY ON THE CONFLICT OF LAWS 490-91 (2d ed. 1980).

[7] *See e.g.*, Coogan, *Security Interests in Investment Securities under Revised Article 8 of the Uniform Commercial Code*, 92 HARV. L. REV. 1013 (1979).

a loan does not constitute a "sale" of the collateral to the lender for purposes of the federal securities laws.

The use of an economic reality test is consistent with this Court's decisions on other questions involving the applicability of federal securities law. *See, e.g., Teamsters* v. *Daniel,* 439 U.S. 551, 558-59 (1979); *United Housing Foundation* v. *Forman,* 421 U.S. 837, 851-52 (1975). Such a test would promote the uniform application of the federal law in this respect, based upon an understanding of the important but limited purposes of that law.

CONCLUSION

For the reasons stated in this brief, amicus curiae prays that this Court reverse the judgment of the United States Court of Appeals for the Second Circuit.

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CERTIFICATE OF SERVICE

I hereby certify that on this 27th day of June, 1980, three copies of the foregoing Brief for Bossier Bank & Trust Company as Amicus Curiae were mailed, postage prepaid, to counsel for petitioner and counsel for respondent as follows: Louis Bender, Bender & Frankel, 225 Broadway, New York, NY 10007; Solicitor General, Department of Justice, Washington, D.C. 20530. Copies of this brief have also this day been mailed, postage prepaid, to all counsel of record in *First National Bank of Las Vegas, New Mexico* v. *Estate of Milton B. Russell, et al.*, No. 80-1401 in the United States Court of Appeals for the Fifth Circuit. I further certify that all parties required to be served have been served.

.....

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